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IN THE SUPREME COURT OF THE UNITED STATES

DIANA BONTÁ, Director, California Department of Health Services, *Petitioner,*

v.

CHILDREN'S HOSPITAL AND MEDICAL CENTER, a Washington corporation, et al., *Respondents.*

ON PETITION FOR WRIT OF CERTIORARI TO THE CALIFORNIA SUPREME COURT

PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

A California statute provides for reimbursement to out-of-state hospitals for care they provide to Medi-Cal recipients. The rate of reimbursement is based on the average paid to California hospitals that enter into contracts with the state. Does this payment scheme violate the Commerce Clause or the Equal Protection Clause?

PARTIES

The petitioner is Diana M. Bonta, Director of the California Department of Health Services. The respondents are Children's Hospital and Medical Center, a Washington corporation; Desert Springs Hospital, Inc., a Nevada corporation; IHC Hospitals, Inc., a Utah corporation, dba Primary Children's Medical Center; Mckenzie-williamette Hospital, an Oregon corporation; Mercy Healthcare Arizona, Inc., an Arizona corporation, dba St. Joseph's Hospital And Medical Center; Merle West Medical Center, an Oregon corporation; National Jewish Center For Immunology And Respiratory Medicine, a Colorado corporation; Peacehealth, a Washington corporation, dba Sacred Heart General Hospital; Rogue Valley Medical Center, an Oregon, Samaritan Health System, an Arizona corporation, dba Desert Samaritan Medical Center, Good Samaritan Regional Medical Center, Havasu Samaritan Regional Hospital, Maryvale Samaritan Regional Hospital, and Thunderbird Samaritan Medical Center; St. Mary's Regional Medical Center, Inc., a Nevada corporation; Washoe Medical Center, Inc., a Nevada corporation; Western Health Network, Inc., a North Dakota corporation, dba Mesa Lutheran Hospital; and Yuma Regional Medical Center, an Arizona corporation

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IN THE SUPREME COURT OF THE UNITED STATES

No.

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v.

CHILDREN'S HOSPITAL AND MEDICAL CENTER, a Washington corporation, et al., *Respondents.*

OPINION OR JUDGMENT BELOW

The opinion of the California Court of Appeal, dated April 15, 2002, is reported at 97 Cal.App.4th 740 (2002). It is reproduced at Appendix A. The order of the California Supreme Court denying review, dated August 14, 2002, is reproduced at Appendix B. 2002 LEXIS 5484.

STATEMENT OF JURISDICTION

The California Court of Appeal opinion implicates the Commerce Clause and the Equal Protection Clause of the United States Constitution. Accordingly, this Court has jurisdiction pursuant to 28 U.S.C. §1257(a) and Rule 10(c) of the Supreme Court Rules.

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

1. Article I, § 8, cl. 3 of the U.S. Constitution, provides that "[t]he Congress shall have power . . . 3. To regulate commerce with foreign nations, and among the several States, and with the Indian tribes;"

2. The Fourteenth Amendment to the U.S. Constitution, § 1 states as follows:

> Section 1. All persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the State where they reside. No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the Unite States; nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

3. Article I, § 7 of the California Constitution, provides for equal protection of the laws. The full text of this provision is reproduced at Appendix C.

4. California Welfare and Institutions Code section 14105.15(i) states as follows:

> Notwithstanding any other provision of law, reimbursement for out-of-state acute inpatient hospital services provided to Medi-Cal beneficiaries shall not exceed the current statewide average of contract rates for acute inpatient hospital services negotiated by the California Medical Assistance Commission or the actual billed charges, whichever is less.

STATEMENT OF THE CASE

This case was brought by 11 out-of-state hospitals that challenged the manner by which California reimbursed them for rendering medical services to California Medi-Cal recipients. The original four-page complaint made no mention of the Commerce Clause or the Equal Protection Clause. The trial court, however, ruled that both constitutional provisions were violated and these rulings, particularly on the Commerce Clause, became the focal point of the Court of Appeal's decision. The California Supreme Court declined to Review the lower court's holding.

When a California resident who is on Medi-Cal travels to another state and needs emergency inpatient hospital care, the out-of-state hospital that provides such care is entitled to reimbursement from the Medi-Cal program. *See* Cal.Code Regs., tit. 22, §51006.[1/] This case concerns the validity of the rate that California pays to those hospitals. The statute that sets forth the applicable rate is California Welfare and Institutions Code section 14105.15(i).[2/] That law provides that California must pay out-of-state hospitals a rate not exceeding the average of what it pays to California contract hospitals.[3/] This formula

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1. As set forth in §51006, California pays for certain other hospital services but emergency care is perhaps the most prominent.

2. Although the statute gives the Department of Health Services (DHS) discretion to pay less than the average, it has chosen to pay hospitals the *maximum* permitted by the statute.

3. Approximately 250 California hospitals negotiate reimbursement rates with the California Medical Assistance Commission (CMAC) for the services they provide to Medi-Cal beneficiaries. These hospitals are generally urban hospitals that

results in a payment rate to out-of-state hospitals that exceeds the rate paid to 58% of California contract hospitals

The heart of the state Court of Appeal's opinion is its conclusion that California's Medi-Cal reimbursement scheme for out-of-state hospitals violates the Commerce Clause. In making this ruling the court engaged in an unwarranted expansion of the meaning of the term "interstate commerce." Contrary to every reported Commerce Clause case, it ruled that a statute violates the negative sweep of the Commerce Clause even when it places no burden on interstate commerce. The court also expanded the law concerning impermissible burdens on interstate commerce. It announced a novel principle that a state must not only refrain from imposing burdens on commerce but must also consider special circumstances of out-of-state facilities. According to the court, these special circumstances might warrant favored treatment of out-of-state facilities over in-state institutions.

REASONS FOR GRANTING THE WRIT

I.

THE COURT OF APPEAL'S DECISION CONFLICTS WITH THIS COURT'S COMMERCE CLAUSE DECISIONS

When California reimburses in-state hospitals it does so in one of two ways: a) The state enters into contracts with hospitals that provide approximately 90% of Medi-Cal services. There is a special commission (CMAC) that negotiates these

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provide 90% of hospital inpatient services under the Medi-Cal program.

agreements with each hospital individually; b) for the balance of the hospitals (mostly small rural hospitals) the state has a complex formula which involves cost data, peer grouping, audits, and other factors. *See* 97 Cal.App.4th 740, 747-748.

California cannot use the payment approaches described above for reimbursing out-of-state hospitals. Most out-of-state hospitals treat Californians only on an episodic basis. In those cases it would be unreasonable to expect California to enter into contracts or apply the complex formulas used for non-contract in-state hospitals. For example, if a hospital in Nebraska happens to treat a single transient California resident in a year, it would be unreasonable to contend that California should negotiate a contract with that hospital[4/] or demand cost data and the opportunity to audit the institution.

To deal with the unique situation of out-of-state hospitals the California Legislature devised a system that is both fair and elegantly simple. It provides that out-of-state hospitals will be paid the average rate paid to California contract hospitals. Welf. & Inst. Code, §14105.15(i).[5/] As we have noted, this results in payments to out-of-state hospitals that

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4. California could hardly negotiate a contract with the 7,500 or so hospitals in this country in anticipation of their treating an occasional California visitor. Nor would it make sense for California to negotiate a contract with a hospital *after* it has already rendered its services to the patient from California.

5. Averaging is a common technique used in many California programs. *See, e.g.*, Cal. Code Regs. tit. 2, §1809 (c)(3), §1865.30 (c)(3), Cal. Code Regs., tit.4, §103, Cal. Code Regs. tit. 5, §15387, Cal. Code Regs. tit.8, §1529, Cal. Code Regs. tit.18, §473, and Cal. Code Regs. tit. 22, §66264.1034.

exceed the rate paid to 58% of California contract hospitals. In many cases, the payments are greater than the hospital would receive from its own state for medicaid services.

In short, because the situation of out-of-state hospitals is different from that of in-state hospitals, the system for paying them is different. It is designed to suit the circumstances. It is different but not invidious, and it does not discriminate against out-of-state hospitals or burden interstate commerce.

The United States Constitution confers authority on Congress to regulate interstate commerce. The Commerce Clause, however, has another aspect. It has a negative sweep, forbidding burdens on interstate commerce that have the effect of discriminating against out-of-state interests in favor of local interests. Where there is a flow of people, goods or services, from one state to another, the receiving state cannot impose a burden on the out-of-state interest in order to further an in-state interest. The doctrine evolved to prevent "economic retaliation" between the states and to control their "mutual jealousies and aggressions." *Baldwin v. G.A.F. Seelig,* 294 U.S. 511, 522 (1935). Here there are no "mutual jealousies" nor is there "economic retaliation," invidious discrimination, or an impermissible burden on interstate commerce.

The California court, however, determined that this Court's decisions compelled a different result. We believe the lower court misinterpreted and improperly expanded the holdings of this Court in the relevant Commerce Clause cases. In all of the cases relied on by the state court, there was a burden placed on interstate commerce. In many cases, local interests benefitted from the imposition of the burden. In other cases the home state was trying to implement a governmental policy at the expense of out-of-state interests. The recurrent theme of these cases, however, was that, whether competition was involved or not, an impermissible burden was imposed on

interstate commerce.

The California court relied on a sentiment expressed on this court over 20 years ago to the effect that jurisprudence in this area was "hopelessly confused," citing *Kassel v. Consolidated Freightways Corp. of Delaware*, 450 U.S. 662, 703 (1981) (Rehnquist, J., dissenting). The state court in this case said, "our high court has yet to provide a fully coherent theory of the negative dimension of the Commerce Clause . . ." 97 Cal.App.4th at 761. The court, however, failed to cure the omission it described. Instead, it misinterpreted this Court's decisions regarding the Commerce Clause and contributed to the confusion in this area of the law.

A few examples illustrate our point. Among others, the California court cited the case of *Camps Newfoundland/Owatonna, Inc. v. Town of Harrison*, 520 U.S. 564 (1997), that involved a Maine statute that provided a general exemption from certain taxes for charitable institutions incorporated within the state. However, a more limited exemption applied to camps which catered principally to out-of-state residents. This had the effect of penalizing or burdening out-of-state campers because they would be charged higher fees than in-state campers. The action of the state had the effect of impermissibly burdening interstate commerce.

Let us pause for a moment to examine what effect the Court of Appeal's decision here would have had in the Maine case. Suppose that the Maine law in the *Camps* case provided the identical general tax exemption to all charitable entities. The state court decision in the instant case could be used to argue that the Commerce Clause requires that an even better tax break be given to entities that serve mainly out-of-state persons if justified by specific facts. If, for example, the out-of-state campers had higher travel costs to the Maine camps, under the court's reasoning, the camps catering to these nonresidents

would presumably be entitled to a higher tax break than the ones catering to Maine residents.

In the Maine case all of the camps were located in Maine. The problem arose when a burden was levied affecting out-of-staters coming into Maine. Here, by contrast, the out-of-staters who are coming into the plaintiffs' states, i.e., Medi-Cal beneficiaries, are not burdened at all. They will receive needed services irrespective of the rates paid to plaintiffs. That is the key difference between this case and the *Camps* case.[6]

In *New Energy Company of Indiana v. Limbach*, 486 U.S. 269 (1988), an Ohio statute granted a tax credit against the state motor vehicle fuel sales tax for ethanol produced in Ohio but not to ethanol produced out-of-state. The court said this was discrimination against out-of-state ethanol producers who sold their product in Ohio.

Again, let us look at the effect the Court of Appeal's decision here might have had on the *New Energy* case. Suppose that the Ohio statute described above had granted an identical tax credit against the fuel tax for all ethanol regardless of state of production. The California court's decision could be used by out-of-state ethanol producers to argue that given their unique circumstances (e.g., higher costs of selling their product in Ohio) they should get a more favorable tax credit than Ohio producers of ethanol.

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6. We are aware that this Court has granted certiorari in a Maine case involving the dormant Commerce Clause and the Medicaid program. *Pharmaceutical Research and Manufacturers of America v. Concannon*, No. 01-188. This case is dissimilar to the Maine case and merits this Court's separate consideration.

The Court of Appeal's decision here turns the law set forth in this Court's Commerce Clause cases on its head. It says, in effect, that not only must California's payment system be free of discrimination but that it must *favor* out-of-state hospitals over in-state institutions. The court discusses the various problems faced by out-of-state facilities-- high costs, etc.-- and concludes that California must pay them at a rate which exceeds that which is paid to in-state hospitals. *See, e.g.*, 97 Cal.App.4th at 766.

Moreover, in a further unwarranted expansion of the Commerce Clause, the Court of Appeal indicates that hospitals that are close to California deserve more favorable treatment than that given to more distant hospitals. 97 Cal.App.4th at 760.

The only interstate aspect of this factual situation is the travel of California residents to other states. These travelers are not burdened in any way by California's reimbursement system. They receive needed medical services because federal law requires that hospitals provide them.

If there is no burden on people traveling interstate, it must be determined whether the other parties to the transaction, the out-of-state hospitals, are also engaged in interstate commerce and whether a burden is placed on them. To begin with, those hospitals are not engaged in interstate commerce. They provide their services in their home state, not in California; they do not send in their doctors to or maintain facilities in California. In the absence of a flow of goods or services across state lines and in the absence of an adverse impact on people coming into their respective states, Welfare and Institutions Code section 14105.15, subdivision (i), does not burden interstate commerce.

Furthermore, even if the out-of-state hospitals are

deemed to be engaged in interstate commerce, California does nothing to discriminate against them. The state places no burden on that commerce. The payments do not result in any windfall or advantage for in-state hospitals, and California is not favoring in-state institutions over out-of-state facilities. There is no "purposeful economic protectionism." Regan, *The Supreme Court and Economic Protectionism: Making Sense of the Dormant Commerce Clause*, 84 Mich. L. Rev. 1091, 1092 (1986). California uses one methodology to pay in-state contract hospitals, it uses another to pay non-contract in-state facilities, and a third to pay out-of-state hospitals. Each payment system is designed to suit the particular circumstances of the group being paid.

If it is determined that there is an impact on interstate commerce, the effect is incidental and is far outweighted by the benefits of the payment system. Accordingly, the statute meets the criteria set forth in *Pike v. Bruce Church,* 397 U.S. 137, 142 (1970).

This Court's decisions do not support the conclusion of the state court that the Commerce Clause may be extended to compel higher payments to out-of-state hospitals than to in-state hospitals. As we have pointed out, 90% of hospital inpatient services provided to Medi-Cal patients in California are provided at hospitals that negotiate a reimbursement rate with the state. Out-of-state hospitals are paid the average of these rates. This results in their being paid at a rate higher than that received by 58% of in-state contract hospitals. The state court, however, hold that this rate is not high enough, that the out-of-state hospitals must receive even more, based on their costs and other factors. This Court should grant certiorari to review this startling extension of the Commerce Clause.

After setting forth the various findings and conclusions of the trial court (97 Cal.App.4th at 759-760), the

Court of Appeal remarked that the hospitals in this case are close to California and are more adversely affected by California's payment system than more distant hospitals. *Id.* at 760. Without saying so explicitly, the court apparently advocates disparate treatment of hospitals close to California versus hospitals located in areas that do not border California. There is no rule of law that would enable California to treat hospitals "close to the California border" one way and more distant hospitals another. For one thing, how close is "close to the California border"? Five miles? Fifty miles? Must California make graduated payments based on distance from California? For another, should California pay more money to border hospitals than to others simply because they treat more Medi-Cal patients? Such discrimination based on volume or proximity would clearly be invalid.

In short, the Court of Appeal has concluded that it is not sufficient that California pays out-of-state hospitals more than it pays over half the contract hospitals within the state. The court concluded that out-of-state hospitals should be *favored* over in-state institutions because of such factors as cost-mix, volume, lack of appeal procedures, and effect on their non-Medi-Cal business. Nothing in Commerce Clause jurisprudence justifies such favored treatment.

The Court of Appeal decries the lack of procedures for out-of-state hospitals to challenge the adequacy of reimbursement rates, indicating that this impermissibly burdens interstate commerce. But the fact is that there is no reason for administrative procedures to challenge payment rates. The rates are fixed by statute. DHS obtains the most recent statewide average contained in CMAC's report to the Legislature. Welf. & Inst. Code, §14165.9(d)(1). That number is applied automatically whenever an out-of-state hospital treats Medi-Cal recipients. There is nothing to appeal, nothing to challenge. (There is an administrative procedure to correct arithmetic

mistakes or a clerical errors.)

And why should out-of-state hospitals have administrative remedies that are not available to California contract hospitals? In fact, there are no administrative procedures that California contract hospitals can invoke to challenge payment rates. Since they negotiate a rate, there is nothing to challenge and such procedures would be superfluous. As is the case with out-of-state hospitals, the rate is set and that's it. Put another way, out-of-state hospitals are in the same position as California hospitals which provide 90% of hospital inpatient services under Medi-Cal. In both situations administrative procedures to challenge rates would be superfluous. Again, the state court improperly extended the reach of the Commerce Clause, commanding that out-of-state hospitals receive favored treatment over the majority of in-state hospitals.[7]

Footnote 15 (97 Cal.App.4th at 764) deserves special attention. In that footnote the court suggests that California can enter into contracts with "the relatively few large hospitals in nearby regions of adjacent states." As we have noted earlier, this is expressly forbidden by statute. Welf. & Inst. Code §14086(b). Second, requiring such procedures would discriminate against hospitals that are more distant. Moreover, there are no standards to determine which hospitals would be suitable for contracts. What is a "large hospital"? How close to California must a hospital be to qualify for contracting? The court suggests those hospitals would be willing to provide cost

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7. Appellate procedures do make sense with respect to the California hospitals that are not on contract. Those hospitals often have disputes with the Department concerning cost data, audit results, overpayments, underpayments, etc. and procedures are necessary to resolve those differences.

data and submit to audits. There is absolutely nothing in the record to support this suggestion. Moreover, the court offers no alternative in the event the hospitals refuse to provide such data or to submit to audits.

Hospitals in all states must treat patients who need emergency care. 42 U.S.C. §1395dd. When a hospital in Montana, for example, treats a California resident, the service is rendered in Montana. The hospital is not competing with any California hospitals for the business of providing services to Medicaid patients. The Montana hospital is providing services that it is obligated to provide and it is doing so within its own state. No California hospital gains any advantage over the Montana hospital by virtue of the amount paid by California to the Montana hospital. The court below conceded this point.[8/]

To avoid the ineluctable conclusion that in-state interests are not favored over out-of-state interests, the court shifts the focus of the debate. Instead of limiting the focus to Medicaid patients- which is the subject of this lawsuit- the court states that a number of the plaintiff hospitals compete for non-Medi-Cal patients, i.e., fee-paying patients, and that their under-compensation for Medi-Cal patients places their other business at a competitive disadvantage. 97 Cal.App.4th at 766. There are a number of responses to this attenuated position.

1) The hospitals in this case never presented evidence showing that their non-Medicaid business was adversely affected by California's Medi-Cal payments and there are no trial court findings to support this assertion. Indeed, the Court

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8. Curiously, the lower court devotes virtually its entire attention to hospitals that are in states contiguous to California. We have no idea what principles or analysis the court would apply to the Montana hospital in our hypothetical.

of Appeal cites nothing to support this premise. The court says the only way out-of-state hospitals can compensate for their unreimbursed costs relating to Medi-Cal "is either to charge other patients more" or accept lower profit margins. *Id.* There is nothing in the record or any trial court finding to support that proposition; it is nothing more than unsupported speculation by the court.

2) Medi-Cal patients at Washoe County Hospital in Reno, the biggest of the plaintiff institutions, comprise only one tenth of one per cent (.01%) of the hospital's patient census. It is hard to believe that this negligible percentage could have any meaningful impact on the hospital's revenue from other sources.[9/] It is thus misleading for the court to characterize the payments made as "under-compensation."

3) The court mixes apples and oranges. The focus in this case is on Medi-Cal, i.e., how California pays out-of-state hospitals for providing care to Medi-Cal recipients versus how California pays California hospitals when they provide such care to Medi-Cal patients. The question is whether in-state hospitals gain some kind of advantage over out-of-state hospitals when both treat Medi-Cal patients. Apples to apples means comparing Medi-Cal to Medi-Cal. It does not mean examining whether Medi-Cal reimbursement rates paid to hospitals close to California have an impact on the hospitals' competition with California hospitals for fee-paying patients. Once again, the Court of Appeal has elasticized the Commerce Clause in a manner that cannot be reconciled with this Court's decisions.

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9. Washoe serves more Medi-Cal patients than any of the other plaintiffs. If its percentage is one tenth of one per cent, the percentage for the other hospitals, which are farther from California, is likely to be even lower.

II.

THE COURT OF APPEAL WRONGLY NARROWED THE MARKET-PARTICIPATION EXCEPTION

In a number of cases this Court has articulated what is known as the market-participation exception. The California court in this case failed to apply that principle accurately. That exception states that when a state is involved in purchasing or selling goods or services, it may favor its local citizens without running afoul of the Commerce Clause. "If a state is acting as a market participant, rather than as a market regulator, the dormant commerce clause places no limitation on its activities." *South Central Timber Dev. v. Wunnicke,* 467 U.S. 82, 93 (1984). This exception means that even if one accepts the lower court's conclusion in this case that the payments by California and its administrative procedures tend to favor California hospitals over out-of-state hospitals, that favoritism is permissible.

The point is illustrated by the Ninth Circuit case of *Big Country Foods v. Board of Education*, 952 F.2d 1173 (9th Cir. 1992). In that case the state of Alaska received federal funds for the purchase of milk for school children. Alaska had a state statute requiring schools receiving state funds to buy dairy products produced in the state of Alaska if the price was no more than 7% higher than products of like quality harvested outside the state. *Id.* at 1175. Pursuant to the statute the Anchorage school district purchased milk from an Alaskan supplier even though the cost was higher than the bid submitted by an out-of-state supplier. The Ninth Circuit noted, "[t]here is no question that Alaska's preference statute discriminates against interstate commerce.... Neither Alaska nor the federal appellees cites any reasons for the statute's existence other than economic protectionism for Alaska's milk harvesters." *Id.* at

1177. Nevertheless the court held that, because of the market-participation exception, there was no Commerce Clause violation.

The Ninth Circuit noted the series of United States Supreme Court cases that establish this exception. For example, in *Hughes v. Alexandria Scrap Corp.*, 426 U.S. 794 (1976), this Court stated, "[n]othing in the purposes animating the commerce clause prohibits a state, in the absence of congressional action, from participating in the market and exercising the right to favor its own citizens over others." (*Id.* at 810.) Similarly in *Reeves, Inc. v. Stake*, 447 U.S. 429 (1980), this Court upheld a South Dakota law which gave favored treatment to South Dakota residents in the purchase of cement. *See also White v. Mass. Council of Construction Employers, Inc.* 460 U.S. 204 (1983).

In *Big Country* the Ninth Circuit also observed that the fact that federal funds were involved did not change the market-participation exception. 952 F.2d at 1180. The court concluded that Alaska was directly involved in the market. It stated,

> In implementing its program to buy milk for its schools, Alaska commits itself to the terms of its annual milk supply contracts, including the obligation to pay for the milk. It also administers the acquisition and disbursement of milk funds through a maze of credits and reimbursements. Federal funds provide the wherewithal to make the milk purchases, but it is Alaska that is the direct participant in the market. Accordingly the market participant exception applies.

Id. at 1180.

Similarly, in the instant case, it is the State of California that participates in the purchase of medical services for those of its residents who require acute inpatient care when out-of-state. Thus, even if this Court concludes that this activity constitutes engaging in interstate commerce, the market-participation exception applies.

The Court of Appeal states that the exception is inapplicable because "the state itself is not a consumer of the service in question, nor does it pick and choose service providers"? 97 Cal.App.4th at 768. This statement enunciates a new principle. The fact that the state does not purchase services for governmental purposes does not mean the exception is inapplicable. The state is purchasing medical services for its citizens both within California and in other states. In this respect the facts here are similar to those in the *Big Country Foods* case. In both cases the state was purchasing something for its citizens– here it is medical services; in *Big Country Foods* it was milk for Alaska's schoolchildren.

The Court of Appeal held that the exception was inapplicable here because "[the state] is not participating in an open market."[10/] *Id.* Here again the court was unfaithful to the decisions of this Court. There is nothing in the case law that requires an "open market" for the exception to apply. When a state steps in and imposes special burdens or requirements, it alters the so-called "open market." This was true in the *Big Country Foods* case. It was also true in *Hughes v. Alexandra*

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10. On the one hand, the Court of Appeal says that the state is not competing in the marketplace but rather acting as a regulator. 97 Cal.App.4th at 768. On the other hand it maintains that the alleged under-compensation by California has an adverse effect on competition between in-state and out-of-state hospitals. *Id.* at 766. The court cannot have it both ways.

Scrap Corp., 426 U.S. 794 (1976). In that case the state of Maryland imposed different documentation requirements on out-of-state companies who sought a bounty for junk cars delivered to in-state processors. Maryland clearly was "not participating in an open market." Indeed, it was altering the conditions of the open market. This court noted that "[the] practical effect was substantially the same as if Maryland had withdrawn altogether the availability of bounties on hulks delivered by unlicensed suppliers to licensed non-Maryland processors." *Id.* at 803, n.13. Despite this interference with the market, the Court held that the exception applied.

III.

THE STATE COURT OPINION DOES NOT REST ON AN INDEPENDENT STATE GROUND

Respondents may argue that the Court of Appeal opinion stands, in part, on an independent state ground and this Court should therefore deny the petition. The lower court did say that the statute in question violates both the state and federal Equal Protection Clauses. However, the court failed to make the "plain statement" required to defeat jurisdiction. The state court simply said the state's "conduct therefore infringes respondents' rights under the equal protection clauses of the state and federal Constitutions." 97 Cal.App.4th at 771. This does not constitute the "plain statement" required by *Michigan v. Long*, 463 U.S. 1032, 1042 (1983), for the state court decision to rest on independent and adequate state grounds.

The principal holding of the state court in this case is not based on state grounds. It is based on the conclusion that the state statute violates the Commerce Clause. On the equal protection issue, the court acknowledged that "[t]he provisions of the California Constitution guaranteeing equal protection . . . are 'substantially the equivalent of the equal protection

clause of the Fourteenth Amendment. . . .' " 97 Cal.App.4th at 769. Moreover, the court relied almost exclusively on federal cases, not state cases, in its equal protection analysis. Under these circumstances, there exists no true independent and adequate state ground barring certiorari. *See New York v. Class*, 475 U.S. 106, 109 (1986) ["The opinion of the New York Court of Appeals mentioned the New York Constitution but once, and then only in conjunction with the United States Constitution."]; *Delaware v. Prouse*, 440 U.S. 648, 653 (1979); *Zacchini v. Scripps-Howard Broadcasting Co.*, 433 U.S. 562, 568 (1977).

IV.

THE STATE COURT OPINION CONFLICTS WITH THIS COURT'S DECISIONS ON EQUAL PROTECTION.

The Court of Appeal acknowledged that there is no fundamental interest involved here and that the rational basis test applies. It then ruled that there was no rational basis for California reimbursement system. In doing so it established new parameters for that test. Contrary to existing law, it shifted the burden of proof to the state and ruled out any considerations of practicality, cost, or administrative necessity.

The rational basis test requires us to examine the state purpose and whether the legislation under scrutiny is a reasonable method of achieving that purpose. *Board of Trustees of the Univ. of Alabama v. Garrett* 531 U.S. 356 (2001). The state purpose here is to reimburse out-of-state hospitals for taking care of California residents who are on Medi-Cal. The question is whether section 14105.15(i) is a reasonable way to do that.

The Court of Appeal conceded that the state is not required to achieve mathematical precision in its payment

scheme. 97 Cal.App.4th at 769. However, it then concluded that California's failure to obtain cost data for out-of-state hospitals means there is no rational basis for our payment scheme.

The Court of Appeal again appears to be saying that hospitals close to California deserve special treatment. *Id.* at 770. The court does not deal with more distant hospitals and provides no guidance as to how close a hospital must be to California to merit payments higher than those paid to California hospitals.

The lower court concludes that "DHS has failed to demonstrate that its differential treatment of respondent hospitals on the basis of their location out of state is rationally related to a legitimate governmental purpose." Contrary to existing law, the court placed the burden on the state to demonstrate that the legislation has a rational basis. "Rather, the burden is upon the challenging party to negative 'any reasonably conceivable state of facts that could provide a rational basis for the classification.' [Citations.]" *Garrett*, 531 U.S. at 367.

Whether or not the state had the burden to show rational basis, the fact is that it did make such a showing. It demonstrated that the situation of out-of-state hospitals (both those close to the California border and more distant ones) poses special problems. For that reason the California Legislature designed a payment system that is different from that used for in-state facilities but that is practical and fair and takes into consideration the special circumstances of out-of-state institutions.[11/] "The problems of government are practical

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11. In a case decided this year, the Fourth Circuit considered an equal protection attack on a Virginia statute that

ones and may justify, if they do not require, rough accommodations--illogical, it may be, and unscientific. [Citation.] A statutory discrimination will not be set aside if any state of facts may reasonably be conceived to justify it. [Citation.]" *Dandridge v. Williams,* 397 U.S. 471, 485 (1985).

The Court of Appeal's ruling that administrative and budgetary considerations merit no consideration is at odds with this Court's holdings. In *Weinberger v. Salfi,* 422 U.S. 749, 780 (1975), the Court discussed a statute and noted that "any imprecision from which it might suffer was justified by its ease and certainty of operation." It also stated that a payment scheme may take into account "the expense and other difficulties of individual determinations." *Id.* at.777; *see also Geduldig v. Aiello,* 417 U.S. 484, 495-496 (1974); *Colorado Health Care v. Colorado Department of Social Services,* 842 F.2d 1158, 1168, 1169, n. 9 (10th Cir. 1988) [costs involved in implementing a program are a valid consideration]; *Mississippi Hosp. Assoc. v. Heckler,* 701 F.2d 511, 518 (5th Cir. 1983). The state court in this case wrongly rejected these principles.

The system designed by the California Legislature has a rational basis. It avoids the problems created by attempting to apply to out-of-state hospitals the methods used to pay in-state hospitals. At the same time it assures that out-of-state institutions will receive a fair and generous payment. In some cases the system may pay an out-of-state hospital more than it would be paid by its home state; in other cases, it may pay less.

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treated tobacco manufacturers in different ways. The court sustained the statute, noting, "[e]ven though the tobacco manufacturers are treated differently, the differences in treatment are related to their different circumstances, allowing the state to accomplish its legitimate purposes." *Star Scientific Inc. v. Beales,* 278 F.3d 339, 352 (4th Cir. 2002) .

On the whole, however, the system is equitable. At the very least, it has a rational basis and is consistent with equal protection principles.

As this court recently stated, "[w]here a group possesses 'distinguishing characteristics relevant to interests the State has the authority to implement,' a State's decision to act on the basis of those differences does not give rise to a constitutional violation. [Citation.]." *Garrett,* 531 U.S. at 366-367. Plaintiffs never met their burden in this case. They never showed there were no conceivable facts that would support the conclusion that the state statute had a rational basis. Accordingly, the court below was wrong in concluding that there was an equal protection violation.

V.

THE QUESTION PRESENTED IS OF NATIONAL IMPORTANCE

All states face the problem of reimbursing out-of-state facilities for care rendered under the circumstances presented here. The payment systems used vary among the states. In states where those systems differentiate between in-state hospitals and out-of-state hospitals, the California decision could jeopardize those reimbursement schemes. Health facilities across the country are in a constant quest for additional revenue, and the instant California decision may be used to further that goal at the expense of effective government.

CONCLUSION

The state Court of Appeal failed to follow this Court's decisions, altering and impermissibly expanding the standards applying to Commerce Clause and equal protection jurisprudence. The decision disregards the law developed by

this Court and has the potential for disrupting many state Medicaid programs. The California system for reimbursing out-of-state hospitals imposes no burden on interstate commerce and does not discriminate against out-of-state institutions. To the extent the payment system might otherwise be deemed burdensome, the statute at issue qualifies for the market-participation exception.

Finally, the state court incorrectly applied this Court's rulings on the Equal Protection Clause. Had it done so correctly, it would have been compelled to find that there is a rational basis for California's reimbursement scheme.

For the reasons stated, this petition for certiorari should be granted.

Dated: November 8, 2002

Respectfully submitted,

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(2)

No. 02 840 NOV 8 2002

OFFICE OF THE CLERK

IN THE SUPREME COURT OF THE UNITED STATES

DIANA BONTÁ, Director, California Department of Health Services, *Petitioner,*

v.

CHILDREN'S HOSPITAL AND MEDICAL CENTER, a Washington corporation, et al., *Respondents.*

ON PETITION FOR WRIT OF CERTIORARI TO THE CALIFORNIA SUPREME COURT

APPENDIX TO PETITION FOR WRIT OF CERTIORARI

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[No. A094061. First Dist., Div. Two Apr. 15, 2002.]

CHILDREN'S HOSPITAL AND MEDICAL CENTER et al., Plaintiffs and Respondents, v.
DIANA BONTÁ, as Director, etc., et al., Defendants and Appellants.

Opinion

KLINE, P. J. - Respondents, 11 out of state hospitals[1] that have provided services to California residents, covered by the Medi-Cal program, commenced this action against appellants, Director of the State Department of Health Services, and the Department itself (collectively DHS or Department), claiming that the difference between the reimbursement of in-state and out-of-state hospitals for costs incurred in the treatment and care of Medi-Cal beneficiaries violated not just state and federal laws but the commerce clause (Commerce Clause) (U.S. const., art. I § 8, cl. 3) and equal protection provisions of the federal and state Constitutions. The trial court agreed with respondents, awarded damages and granted respondents prejudgment interest and attorney fees. We shall lower the amount of prejudgment interest allowed but otherwise affirm the judgment.

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1. Respondent hospitals are: Washoe Medical Center in Reno, Nevada; St. Mary's Regional Medical Center (Reno, Neva.); rogue Valley Medical Center (Medford, Ore.); St. Joseph's Hospital and Medical Center (Phoenix, Ariz.); Desert Samaritan Medical Center (Mesa, Ariz.); Good Samaritan Regional Medical Center (Phoenix, Ariz.); Maryvale Samaritan Medical Center (Phoenix, Ariz.); Thunderbird Samaritan Medical Center (Glendale, Ariz); Mesa Lutheran Hospital (Mesa, Ariz.); and Desert Springs Hospital (Las Vegas, Nev.) Seven smaller out-of-state hospitals with lesser claims which are originally named as plaintiffs were dismissed from the action during the trial.

STATEMENT OF THE CASE AND FACTS

The state Medi-Cal program effectuates the federal Medicaid program established under title XIX of the Social Security Act (42 U.S.C. § 1396 et seq.) (the Medicaid Act), which authorizes the payment of federal funds to states to defray the cost of providing medical assistance to low-income persons. (See *Rite Aid of Pennsylvania, Inc. v. Houstoun* (3d Cir. 1999) 171 F.3d 842, 845.) The state reimburses California hospitals for services to Medi-Cal beneficiaries in one of two ways: (1) according to a specific contractual rate of payment negotiated between the hospital and the California Medical Assistance Commission (CMAC); or (2) on the basis of actual costs, calculated by formulas set forth in the California Code of Regulations. (Cal. Code Regs.,[2] tit. 22, §§ 51536, 51539, 51541, 51546, 51549.) California hospitals that have not negotiated contracts with CMAC, and are reimbursed on the basis of their actual costs, are paid the lesser of (1) their customary charges; (2) allowable costs determined by the Department; (3) the "[a]ll inclusive rate per discharge limitation" (ARPDL);[3] or the (4) the "peer grouping rate per discharge limitation" (PGRPDL).[4] (Tit. 22, § 51546, subd. (a).)

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2. All further references to regulations will be to the California Code of Regulations unless otherwise specified.

3. The "[a]ll-inclusive rate per discharge" (ARPD) is the "per discharge dollar limit on Medi-Cal reimbursable costs prior to the application of the peer grouping inpatient reimbursement limitation." (Tit. 22, § 51545, subd. (a)(4).) The ARPDL is the all-inclusive rate per discharge multiplied by the number of Medi-Cal discharges. (Tit. 22, § 51545, subd. (a)(5).)

4. The "peer grouping rate per discharge limitation" is the "60th percentile ARPD of each provider's peer group multiplied by the provider's number of Medi-Cal discharges." (Tit. 22, § 51545, subd. (a)(71).) The "peer group" is "a group of hospitals with similar characteristics that are

The complex formulas used to determine the reimbursement to which noncontract California hospitals are entitled require development of an input price index (consisting of "a market basket classification of goods and services purchased by hospitals, a corresponding set of market basket weights derived from each hospital's own mix of purchased goods and services, and a related series of price indicators" (tit. 22, § 51536, subd. (g))[5] and a hospital cost index (consisting of "an input price index and an allowance for changes in service intensity").[6] (Tit. 22, § 51536, subd. (f).) The regulations also require classification of hospitals' fixed and variable costs, application of an annual service intensity allowance and volume adjustment in certain circumstances. In-state hospitals are placed into one of 36 enumerated peer group categories (tit. 22, § 51553) and reimbursement is payable "at no more than the 60th percentile rate per discharge of the peer group to which the hospital is assigned by the Department." (Tit. 22, § 51539, subd. (b).) Such hospitals may request administrative

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grouped together for purposes of determining reimbursement limitations." (Tit. 22, § 51545, subd. (a)(69).)

5. "Market basket categories" pertain to such expenses as physicians' salaries, other professional fees, food, drugs, medical instruments and appliances, rubber and plastics, travel, apparel and textiles, and business services. (Tit. 22, § 51536, subd. (g)(3).)

6. "Service intensity" is defined in the regulations (with characteristic prolixity) as "the necessary changes in the character of the services provided to each patient, including changes in applicable technology, qualitative changes in personnel, quantitative changes in personnel, qualitative changes in supplies, drugs, and other materials, and quantitative changes in supplies, drugs, and other materials. Service intensity does not include changes in the types of patients and illnesses treated." (Tit. 22, § 51536, subd. (b)(8).) The sources of the "price indicators" pertinent to each "market basket category" are for the most part either the consumer price index, the producer price index or statistics periodically published by the United States Department of Labor, Bureau of Labor Statistics. (*Ibid.*)

adjustments of the all-inclusive reimbursement rates and limits (tit. 22, §§ 51536, subd. (j), 51539, subd. (d)(1), 51550) and may appeal decisions on administrative adjustments (tit. 22, §§ 51536, subd. (k), 51539, subd. (d)(3)).

The elaborate formulae designed to sensitively determine the costs in-state hospitals incur in treating Medi-Cal patients have no application to out-of-state hospitals that treat such persons. Nor are out-of-state hospitals permitted to negotiate reimbursement contracts with CMAC. The methodology DHS uses to reimburse out-of-state hospitals is prescribed by subdivision (i) of Welfare and Institutions Code section 14105.15, which was enacted in 1992 (hereafter subdivision (i)). This statute provides that "reimbursement for out-of-state acute inpatient hospital services provided to Medi-Cal beneficiaries shall not exceed the current statewide average of contract rates for acute inpatient hospital services negotiated by the California Medical Assistance Commission or the actual billed charges, whichever is less." In addition to their constitutional claims, respondents challenged DHS's application of subdivision (i) on the ground the Department "does not pay out-of-state hospitals the 'current' statewide average of contract rates, but rather uses an average of the different rates paid in-state contract hospitals on December 1 of the previous year." The complaint states that "[i]n an inflationary economy, such as the one that hospitals operate in, last year's average rate is always less than the 'current' rate."

Furthermore, while out-of-state hospitals may request administrative adjustments to the rate of reimbursement, administrative decisions to grant or deny such adjustments may not be appealed and are final. (Tit. 22, § 51543, subd. (b).) This contrasts with the right of in-state hospitals, which may appeal denial of an adjustment administratively and, if need be, judicially. (Tit. 22, § 51539, subd. (d)(3).)

Under the reimbursement methodology used by DHS prior to the 1992 enactment of subdivision (i), out-of-state hospitals were reimbursed "at a percentage of allowable billed charges based on Medicaid information obtained from the Medicaid program for the state of location." (Tit. 22, former § 51543, subd. (a) [amended 1992].) The percentage of reimbursement was determined by one of five alternative methodologies, depending on the extent of the information made available to DHS. (*Ibid.*) Respondents allege, and the trial court essentially agreed, that under the prior reimbursement methodology California paid out-of-state hospitals 65 percent of their charges. Under the new scheme, respondents receive only 38 percent of their charges.

The states in which respondent hospitals are variously located – Nevada, Arizona and Oregon – prohibit them from refusing to treat Medi-Cal patients. (See *Orthopaedic Hospital v. Belshe* (9th Cir. 1997) 103 F.3d 1491, 1498 ["hospitals have a legal obligation to provide those services regardless of the level of Medi-Cal reimbursement rates"].) Because they must treat such persons, respondents have incurred substantial shortfalls in reimbursement based on a comparison of the amounts they now receive to the amounts they would have received under the prior rates.

The Federal Proceedings.

In 1995, before they commenced this state proceeding, respondents and other hospitals filed an action against DHS in the United States District Court for the Northern District of California (*Children's Hosp. and Medical Center v. Belshe*, No. C-95-1076 MHP) alleging that California's reimbursement scheme for out-of-state hospitals did not comply with the so-called Boren Amendment to the Medicaid Act (42 U.S.C. former § 1396a(a)(13)(A); see Historical Notes, 42 U.S.C.A. (2001 supp.) foll. § 1396a, p. 286 [repealed]), and seeking

declaratory and injunctive relief. The federal action sought no damages but only declaratory relief invalidating the existing reimbursement scheme, compelling DHS to replace it with a more equitable system.

Prior to enactment of the Boren Amendment, states that participated in the federal Medicaid program were required to reimburse hospitals for the reasonable cost of providing inpatient services, which was ordinarily accomplished through retrospective payments based on a hospital's costs for specified services. (See *West Virginia University Hospitals, Inc. v. Casey* (3d Cir. 1989) 885 F.2d 11, 15, affd. on other grounds (1991) 499 U.S. 83 [111 S.Ct. 1138, 113 L.Ed.2d 68].) The Boren Amendment required states to prospectively establish reimbursement rates that "are reasonable and adequate to meet the costs which must be incurred by efficiently and economically operated facilities in order to provide care and services.[7/] The measure had two purposes: to encourage health care providers to meet a reasonable rate or absorb the loss if their costs exceeded that rate and to provide states greater flexibility in determining the method of payment. (Sen.Rep. No. 97-139, 1st Sess., p. 478 (1981), reprinted in 1981 U.S. Code Cong. & Admin. News, p. 744; see also *Wilder v. Virginia Hospital Assn.* (1990) 496 U.S. 498, 515 fn. 13 [110 S.Ct. 2510, 2520, 110 L.Ed.2d 455]; *Folden v. Washington State DSHS* (9th

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7. The Boren Amendment required that a state medical assistance plan provide "for payment . . . under the plan through the use of rates (determined in accordance with methods and standards, developed by the State . . . and which, in the case of hospitals, take into account the situation of hospitals which serve a disproportionate number of low income patients with special needs . . .) which the State finds, and makes assurances satisfactory to the Secretary, are reasonable and adequate to meet the costs which must be incurred by efficiently and economically operated facilities in order to provide care and services . . ." (42 U.S.C. former § 1396a(a)(13)(A).)

Cir. 1992) 981 F.2d 1054, 1056.)

In orders dated January 9, 1997, and February 5, 1998, United States District Court Judge Marilyn Hall Patel denied DHS's motion for summary judgment, determined that the procedural and substantive requirements of the Boren Amendment apply equally to in-state and out-of-state hospitals and found that DHS failed to meet its procedural requirements in setting reimbursement rates for out-of-state hospitals. Judge Patel specifically held that DHS did not discharge its obligation under the Boren Amendment to make requisite adjustments in the payments to out-of-state hospitals that "serve a disproportionate share of low-income patients with special needs."

In her 1998 order, Judge Patel noted that in 1997, while the action before her was pending, portions of the Boren Amendment were repealed and revised by section 4711 of the Balanced Budget Act of 1997 (Pub.L. No. 105-33 (Aug. 5, 1997) 11 Stat. 251.) Section 4711 eliminated the "findings" and "assurances" methodology prescribed by the Boren Amendment and required instead that states create a "public process for determination of rates of payment under the [medical assistance] plan." (42 U.S.C. § 1396a(a)(13(A).) Under the new statutes, states must allow "providers, beneficiaries and their representatives, and other concerned State residents" (§ 1396a(a)(13)(A)(ii)) a reasonable opportunity to review and comment on "proposed rates, the methodologies underlying the establishment of such rates, and justifications for the proposed rates." (42 U.S.C. § 1396a(a)(13)(A)(i) (1997).) Section 4711 also requires that rates "take into account . . . the situation of hospitals which serve a disproportionate number of low-income patients with special needs." (42 U.S.C. § 1396a(a)(13)(A)(iv) (1997).) As Judge Patel observed, the foregoing requirements of section 4711 "affect[] only payments made to out-of-state hospitals for items and services furnished on or after October 1,

1997."[8/] However, in December 1997 the Health Care Financing Administration (HCFA), the federal agency responsible for overseeing operation of the Medicaid Program, authorized states to continue to use payment methodology approved under the Boren Amendment methodology, but only with respect to in-state hospitals.

At the end of her 1998 order, Judge Patel allowed that her determination that the Boren Amendment applied to out-of-state hospitals and that the Department failed to comply with its procedural requirements "involves a controlling question of law as to which there may be substantial ground for difference of opinion." Accordingly, she found that an immediate appeal from her orders "may materially advance the ultimate termination of this litigation" and granted the state's petition for an interlocutory appeal under 28 United States Code section 1292(b), certified the action for interlocutory appeal and stayed further district court proceedings pending a decision from the Ninth Circuit Court of Appeals. The Ninth Circuit granted the state's petition for permission to prosecute an interlocutory appeal, and decided the appeal on August 16, 1999. (*Children's Hosp. and Health Center v. Belshe* (9th Cir. 1999) 188 F.3d 1090, cert. den. 530 U.S. 1204 [120 S.Ct. 2197, 147 L.Ed.2d 233].)

In a split opinion, the Ninth Circuit affirmed the judgment of the district court. The majority held that repeal of the Boren Amendment did not render the case moot and the action was not barred by the Eleventh Amendment. Among other things, the majority pointed out that, as authorized by the HCFA, DHS continued to use payment methodologies approved under the

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8. Differences between the Boren Amendment and the 1997 statute that replaced it are spelled out in more detail in *Children's Seashore House v. Waldman* (3d Cir. 1999) 197 F.3d 654, 655-657.

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Boren Amendment even after its repeal, but "refuses, however, to apply that methodology to its reimbursement of out-of-state hospitals for services they provide to Medi-Cal patients." (*Children's Hosp. and Health Center v. Belshe, supra*, 188 F.3d at p. 1095.) The Boren Amendment applied to out-of-state health care providers, but did not require that same methodology to be used to determine reimbursement rates for both in-state and out-of-state providers. (*Id.* at pp. 1096-1099.) As the majority concluded, DHS "has the option of complying with the Boren Amendment or with the public process provisions of the Balanced Budget Amendment of 1997. It doe not have the option of failing to comply with either law. So long as it fails to comply with the Balanced Budget Amendment, it is bound by the Boren Amendment, and *we hold that the Boren Amendment applies to all hospitals, including out-of-state hospitals. We reject [DHS's] contention that the administrative burden of applying the Amendment to out-of-state providers suggests that Congress intended otherwise." Id.* at p. 1099, italics added.)

State Proceedings.

When respondents initiated the federal action they filed a claim for compensation for past underpayments with the State Board of Control. In 1995, after the claim was denied, respondents commenced the present action in the San Francisco Superior Court. Unlike the federal action, which sought only prospective declaratory relief, the state action sought damages for past underpayments. The state proceeding was necessitated by the fact that while a federal court may find that a state official failed to comply with federal statutory and regulatory requirements, and prospectively enjoin such non-compliance, the Eleventh Amendment bars such a court from imposing a liability which must be paid from public funds in the state treasury. (*Edelman v. Jordan* (1974) 415 U.S. 651, 663-665 [94 S.Ct. 1347, 1355-1357, 39 L.Ed.2d 662].) Thus, the complaint

herein states that the present action is necessary "to protect [respondents'] right to receive retroactive damages for DHS' continuing pattern of unlawful underpayments to out-of-state hospitals in connection with their treatment of Medi-Cal patients since at least October 1992."

Unlike the federal complaint, the complaint in this action makes no mention of the Boren Amendment; it simply alleges generally that appellants' reimbursement scheme violated "federal and state law and the California and U.S. Constitution." The only state statute referred to in the complaint is subdivision (i)[9] As earlier noted, respondents allege that DHS's application of that statute—which provides that reimbursement for out-of-state hospitals "shall not exceed the current statewide average of contract of contract rates for acute inpatient hospital services"— is invalid, because DHS does not pay out-of-state hospitals the current statewide average of contract rates, but rather the average rate paid in-state hospitals during the previous year, which in an inflationary economy is always less than the current rate.

On December 9, 1998, respondents moved for summary adjudication of two issues. Maintaining Judge Patel's orders were res judicata (the Ninth Circuit had not yet ruled),

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9. However, in its conclusions of law, the trail court states that "California law mandates that [DHS's] treatment of out-of-state hospitals be 'consistent with the requirements of the Federal Social Security Act' (i.e., the Medicaid Act.)," citing Welfare and Institutions Code section 14122. Section 14122 is not mentioned in the complaint because it does not pertain to the reimbursement of out-of-state hospitals. By its own terms, this statute relates to the "care and treatment, or both, of persons eligible for medical assistance . . . by providers in another state in those cases where out-of-state care or treatment is rendered on an emergency basis or is otherwise on the best interest of the person under the circumstances." The regulations implementing this statute (tit. 22, § 51006) make it even more clear that section 14122 relates only to the nature and quality of Medi-Cal patient care.

respondents contended it must therefore be deemed established that, prior to its repeal, the Boren Amendment applied to California's reimbursement scheme and was violated, so that there was no triable issue as to that question. Respondents claimed there was also no triable issue as to the amount of damages to which they were entitled, because federal law mandates that states may only use reimbursement rates that have been approved by the HCFA. Respondents claimed that, because the federal district court invalidated the DHS's current-rate setting methodology, the former HCFA-approved rate-setting methodology remained in effect and was the only legally effective rate-setting methodology that could properly be employed for purposes of calculating respondents' damages.[10/]

DHS opposed respondents' motion essentially on the grounds Judge Patel's determinations were in the form of interim orders and therefore not binding as res judicata, and that, in any case, Judge Patel found only that DHS failed to comply with the procedural requirement of the Boren Amendment, and never determined the substantive requirement had not been met. On March 9, 1999, respondents' motion for summary adjudication was denied by Judge A. James Robertson II, without a statement of reasons.

On September 13, 1999, about a month after the Ninth Circuit affirmed Judge Patel and remanded the case to her for further proceedings, DHS moved in the superior court to strike portions of the complaint. The motion proceeded on the

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10. This argument relied on *Exeter Memorial Hosp. Ass'n v. Belshe* (E.D.Cal. 1996) 943 F.Supp. 1239, 1243 ("if HCFA were to disapprove the State plan amendment, the State would be required to reimburse providers under the existing plan and would be required to do so retroactively"). See also *Mass. Fed. of Nursing Homes v. Com. of Mass.* (D.Mass. 1992) 791 F.Supp. 899, 905; *Pinnacle Nursing Home v. Axelrod* (W.D.N.Y. 1989) 719 F.Supp. 1173, 1182-1183.

hypothesis that all of respondents' claims, and at least their constitutional claims, were "dependent upon and inextricably tied" to the assertion that appellants violated a federal statute (42 U.S.C. former § 1396a(a)(13)(A)), because except for the Medicaid Act "there is no requirement that California must pay someone who renders care to a California resident." According to DHS, "[i]t is only the [Medicaid Act] and California's participation in the program authorized by that statute, which compels California to reimburse hospitals in such situation." Relying on the holding in *Alden v. Maine* (1999) 527 U.S. 706 [119 S.Ct. 2240, 144 L.Ed.2d 6361] (*Alden*) that the powers delegated to Congress under article I of the United States Constitution do not include the power to subject nonconsenting states to private suits for damages in their own courts unless "there is 'compelling evidence' that the States were required to surrender this power to Congress pursuant to the constitutional design" (*Alden*, at p. 731 [119 S.Ct. at p. 2255]), DHS maintained that respondents' "federally-based causes of action" are barred by the doctrine of sovereign immunity implicit in the Eleventh Amendment, which California has not waived. The motion to strike included the fallback argument that if the trial court believed respondents' state claims were separate and independent of the federal claims, "then, at most, the court should permit [them] to assert only two causes of action: a) alleged violation of the state Constitution, and b) alleged violation of section 14105.15 of the state Welfare and Institutions Code [i.e., subdivision (i)]."

Respondents agreed their damages claims would be barred by the Eleventh Amendment if they derived from a private right of action created by Congress, but claimed they never alleged any such federal claim in this proceeding and were relying instead on "a variety of State-based legal grounds."

On October 19, 1999, DHS's motion to strike was granted by Judge David Garcia in an order stating, without elaboration,

that "all causes of action based on violations of federal law are hereby stricken from the complaint."

On December 10, 1999, DHS moved for summary judgment and, on December 21, 1999, respondents filed a cross-motion seeking the same relief. Judge Garcia denied both motions on January 19, 2000. In denying DHS's motion, Judge Garcia implicitly rejected the contention that respondents were improperly using rulings of the United States District Court and the Ninth Circuit "to mount an indirect attack based on the alleged violation of a federal statute" precluded by *Alden, supra*, 527 U.S. 706.

A bench trail before Judge Robert L. Dondero commenced on July 10, 2000, and lasted 10 days. On December 14, 2000, after posttrial briefing, the trial court issued 26 findings of fact, 32 conclusions of law, and an order. The court concluded that, as alleged in the complaint, DHS violated "state and federal constitutional standards." Deferring to the federal district court ruling, which had by then been affirmed by the Ninth Circuit (*Children's Hosp. and Health Center v. Belshe, supra*, 188 F.3d 1090), the court also concluded that DHS violated the Boren Amendment, indicating that the constitutional and state statutory violations which it found were in part the result of this violation, because the Boren Amendment was in effect during the period for which respondents sought damages. As the federal courts had found that DHS's reimbursement scheme violated the Medicaid Act, the trail court declared that DHS was "collaterally estopped from raising these issues again in that they have already had a full and fair opportunity to litigate them. *Lumpkin v. Jordan* (1996) 49 Cal.App.4th 1223 [57 Cal.Rptr.2d 303]; *Abdallah v. United Savings Bank* (1996) 43 Cal.App.4th 1101 [51 Cal.Rptr.2d 286]."

The trial court found not only that the Medi-Cal patients respondents served were much more costly to treat than Medi-

Cal patients typically served by in-state hospitals, but also that DHS's payments to respondents "have *nothing* to do with costs, acuity, or any of the other important factors that are considered for in-state hospitals" (original italics), that respondents were not reimbursed for costs that were "reasonable" and "allowable" under the Medicaid program and for which in-state hospitals were compensated, and that damages should be calculated by subtracting the amount of compensation respondents received from DHS from the amount they would have received under the reimbursement method prescribed by regulations that had been approved by the HCFA and were used by DHS prior to the enactment of subdivision (i). (Tit. 22, § 51543 (1992).) Using this methodology, the court calculated a net shortfall of $6,088,263 during the period from April 1, 1994 (one year prior to the filing of respondents' claim with the Board of Control) to August 14, 2000, which resulted in reimbursement of 85 percent of the Medi-Cal patient costs respondents incurred during that period. The court also awarded respondents prejudgment interest from August 14, 2000, to the date of judgment calculated at the rate of 10 percent per annum, together with "an award of attorneys fees pursuant to the private attorney general doctrine, in [an] amount to be determined according to proof." (See Code Civ. Proc., § 1021.5.)

After judgment was entered, respondents requested attorney fees in the amount of $1,289,967, which was arrived at by application of a 1.5 multiplier. Rejecting the use of a multiplier, and deducting certain hours claimed by respondents' counsel, the court awarded fees in the amount of $827,145.

This timely appeal followed.

DISCUSSION

The issues we are asked to address —whether DHS's reimbursement scheme violates the Commerce Clause, denies

equal protection of the law, and infringes rights arising under the Welfare and Institutions Code—present questions of law, as do the related questions of the effect of the federal rulings and the application to this case of the Eleventh Amendment. We review such issues independently. (*Crocker National Bank v. City and County of San Francisco* (1989) 49 Cal.3d 881, 888 [264 Cal.Rptr. 139, 782 P.2d 278].)

I.

Eleventh Amendment.

(1) It is necessary, at the outset, to eliminate some confusion as to application of the Eleventh Amendment. If the trial court correctly concluded that the reimbursement scheme is constitutionally defective or violates state statutes, the state would enjoy no immunity under the Eleventh Amendment, as the violations would not pertain to any congressional mandates. However, as noted, in drawing its conclusions as to the violations of constitutional standards and state statutes, the trial court referred to the determination of the federal district court, affirmed by the Ninth Circuit, that DHS violated provisions of the federal Medicaid Act pertaining to the compensation of out-of-state hospitals. In the mind of the trial court, the state statutory and constitutional violations were in some unspecified measure the result of the DHS's failure to comply with procedural and substantive requirements of federal law. DHS argues that the trial court's conclusion that the out-of-state rates paid by the Department violate substantive or procedural requirements of federal law "is inconsistent with the earlier ruling by the court striking all causes of action alleging violations of federal law." According to DHS, "[s]ince *Alden* precludes suit in state court based on a violation of a federal statute, plaintiffs should not be permitted to rely on federal court rulings which were based on violations of a federal statute. They cannot do indirectly what they cannot do directly."

Conceiving respondents' constitutional and state statutory claims to be entirely derivative of federal rulings that it violated federal statutes, DHS suggests, though it does not flatly say, that the claims advanced here by respondents are all barred by the doctrine of sovereign immunity articulated in *Alden, supra*, 527 U.S. 706. The trial court correctly rejected this claim.

Prior to *Alden* most Eleventh Amendment cases involved *federal court* actions against a state on the basis of alleged violations of a *federal statute*. *Alden* was an action in state court by state probation officers against the state under the Fair Labor Standards Act of 1938 (29 U.S.C. § 201 et seq.), which purported to authorized private actions against the state in *state courts* without their consent. The federal statute with which we are here concerned, the Medicaid Act, contains no such provision. Furthermore, *Alden* involved no claimed violations of state or federal constitutional standards or state law. The present action is one in state court in which unidentified federal statutory causes of action (which respondents insist never existed in the first place) were stricken prior to trial and the trial court, which never independently determined whether any federal statute was violated, found violations only of the state and federal constitutional standards and state statutes. The federal statutory violations found by the federal courts relate to the questions whether DHS violated constitutional requirements only because they put the questioned conduct in context; the federal statutes do not, however, provide the legal basis upon which respondents sought and received damages. The Eleventh Amendment only restricts the United States—that is, Congress—from subjecting unconsenting states to lawsuits by citizens of the same or another state. The Medicaid Act was not designed for and does not achieve that proscribed purpose; and the fact that violations of the Medicaid Act may result in or exacerbate violations of constitutional requirements does not in and of itself implicate the doctrine of sovereign immunity. Because the rights asserted by respondents in this action derive

from the Constitution of this state and nation, not from any private right of action crated by Congress, *Alden* does not subject them to the bar of the Eleventh Amendment.

II.

The Commerce Clause.

A.

The Commerce Clause provides that "Congress shall have power . . . ¶ . . . ¶ [t]o regulate commerce . . . among the several states . . . " (2) "It has long been accepted that the Commerce Clause not only grants Congress the authority to regulate commerce among the States, but also directly limits the power of the States to discriminate against interstate commerce. [Citations.]" (*New Energy Co. of Indiana v. Limbach* (1988) 486 U.S. 269, 273 [108 S.Ct. 1803, 1807, 100 L.Ed.2d 302]; *Gibbons v. Ogden* (1824) 22 U.S. (9 Wheat.) 1, 199-200 [L.Ed. 23, 70-71]; *Cooley v. Board of Wardens* (1851) 53 U.S. (12 How.) 299, 319 [13 L.Ed. 996, 1003].)

The United States Supreme Court regularly explains that the implicit or "dormant" limitation on the authority of the states to enact legislation affecting interstate commerce precludes state regulation in certain areas "even absent congressional action." (*CTS Corp. v. Dynamics Corp. of America* (1987) 481 U.S. 69, 87 [107 S.Ct. 1637, 1748, 95 L.Ed.2d 7].) "Though phrased as a grant of regulatory power to Congress, the Clause has long been understood to have a 'negative' aspect that denies the States the power unjustifiably to discriminate against or burden the interstate flow of articles of commerce. [Citations.] The Framers granted Congress plenary authority over interstate commerce in 'the conviction this in order to succeed, the new Union would have to avoid the tendencies toward economic Balkanization that had plagued

relations among the Colonies and later among the State under the Articles of Confederation.' [Citation.] See generally The Federalist No. 42 (J. Madison). 'This principle that our economic unit is the Nation, which alone has the gamut of powers necessary to control of the economy . . . has as its corollary that the states are not separable economic units.' [Citation.] [¶] Consistent with these principles, we have held that the first step in analyzing any law subject to judicial scrutiny under the negative Commerce Clause is to determine whether it 'regulates evenhandedly with only 'incidental' effects on interstate commerce, or discriminates against interstate commerce.' [Citations.]" (*Oregon West Systems, Inc. v. Department of Environmental Quality of Ore.* (1994) 511 U.S. 93, 98-99 [114 S.Ct. 1345, 1349-1350, 128 L.Ed.2d 13].)

The crucial factual determinations the trial court used to support its conclusion that DHS's reimbursement scheme affronted this negative aspect of the Commerce Clause were that (1) the unweighted average of in-state contract rates for acute inpatient hospital services used by DHS as the basis for reimbursing out-or-state hospitals was 23.8 percent lower than a weighted average would be and the use of an unweighted average compensated respondents nearly $3 million less than they would have received if DHS employed a weighted average; (2) in-state contract rates consistently increased over time and that "use of a rate that is set on December 1, and not adjusted until the next year, inevitably results in out-of-state hospitals being paid less than the 'current' average contract rate," as mandated by state law implementing the Medicaid Act (i.e., subdivision (i); (3) DHS annually distributes over $2 billion in disproportionate share adjustments to state hospitals, but "has never made a payment of disproportionate share moneys to any out-of-state hospital", (4) in-state hospitals are entitled to challenge DHS cost determinations administratively and judicially, and DHS is obliged to pay interest on the amounts in-state hospitals are ultimately determined to have been

undercompensated, but out-of-state hospitals cannot similarly challenge the adequacy of the compensation they receive; (5) out-of-state hospitals typically serve Medi-Cal patients who are more costly to treat than the Medi-Cal patients typically treated by in-state hospitals; (6) regardless of the financial disincentives in treating Medi-Cal patients, out-of-state hospitals cannot refuse to treat most Medi-Cal patients, out-of-state hospitals cannot refuse to treat most Medi-Cal patients or transfer them to a California hospital; (7) DHS payments to out-of-state hospitals "have *nothing* to do with costs, acuity, or any of the other important factors that are considered for in-state hospitals" (original italics): (8) during the relevant time period (i.e., April 1, 1994 to August 14, 2000) the expenses incurred by respondent hospitals in treating Medi-Cal patients that were allowable under the principles of cost reimbursement reflected in the Medicaid Act were $22,660.318, but the compensation respondents received for the services they provided such patients during that period were $14,696,955, which was "only sixty-five percent . . . of their 'allowable costs' for the Medi-Cal patients they treated," "leaving a net shortfall based on 'allowable costs' (exclusive of interest) of $7,963,33"; and (9) under the reimbursement system employed by DHS prior to its use of the present system respondents would have received $19,380,433 for the services they provided Medi-Cal patients during the relevant time period, leaving a net shortfall (exclusive of interest) of $4,683,478[11/]

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11. These findings, and particularly the calculation of damages by a methodology different from the reimbursement scheme described by subdivision (i), imply that the trial court found subdivision (i) unconstitutional, either on its fact as DHS maintains, or as applied, as respondents contend. (See Brown-Forman Distillers Corp. v. N.Y. Liquor Auth. (1986) 476 U.S. 573, 579 [106 S.Ct. 2080, 2084, 90 L.Ed.2d 552] ["When a state statute directly regulates or discriminates against interstate commerce, or when its effect is to favor in-state economic interests over out-of-state interests, we have generally struck down the statute without further

The trial court concluded that the "fundamental dissimilarities" if found between the treatment of in-state and out-of-state hospitals adversely affected the commercial health of out-of-state hospitals. As stated by the court, "the evidence shows that [respondents] received compensation that is not even substantially commensurate with the acute care services they are *compelled* to render for Medi-Cal patients because of Medicaid requirements. Also, [respondents] lack the contracting opportunity and review procedures enjoyed by hospitals in California. Such distinctions are discriminatory and violate the [C]ommerce [C]lause." (Original italics.)

The reimbursement methodology DHS has employed since 1992 affected respondent hospitals far more adversely than most other out-of-state hospitals because of the unusually high number of Medi-Cal patients they each treat. Unlike the vast majority of out-of-state hospitals, respondents are located close to the California border and serve bi-state regions encompassing large rural areas of California in which the level of medical care immediately available is considerably lower than that provided by respondents. Thus, the trial court found respondents "provide the full medical services needed for acute care Medi-Cal patients not just visiting the states of Arizona, Oregon or Nevada, but also those Californians who must avail themselves of [respondents' facilities] . . . because they are the closest major trauma centers available to Medi-Cal participants residing in California." (Original italics.) For example, because large

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inquiry."]) Respondents' belief the trial court only found the statute unconstitutional as applied by DHS implies subdivision (i) would create no constitutional problem if the statewide average of contract rates used to calculate the reimbursement of out-of-state hospitals was truly current and weighted to reflect the length of Medi-Cal patients stays. The trial court never indicated whether the statutorily prescribed reimbursement scheme would pass constitutional muster if applied in this manner, an the evidence received by the court does not satisfactorily answer the question.

numbers of Medi-Cal beneficiaries residing in California can so easily reach respondent Washoe Medical Center, located in Reno, Nevada, it treats more Medi-Cal patients than any other hospital in the nation located outside California. Moreover, due to trauma care and other forms of intensive care respondent hospitals provide, they attract "Medi-Cal patients who are much sicker, and therefore require a greater expenditure of resources and costs, than the typical in-state Medi-Cal patient."[12/]

The trial court's view that DHS's constitutionally offensive conduct was at least partly attributable to the violations of the Boren Amendment established in the federal proceedings is shown by the quotation in its order of Judge Patel's statement that DHS "'gathered no information on the costs incurred by out-of-state hospitals and performed no empirical analysis of the effects of the reimbursement scheme on out-of-state hospitals [DHS] therefore failed to provide ant basis for a reasonably principled analysis in determining whether the payment rates that it provides to out-of-state hospitals are "reasonable and adequate.'" The court also referred to Judge Patel's observation that DSH made no disproportionate share adjustment payments to out-of-state hospitals, nor "'made any findings as to whether any out-of-state hospitals serve a disproportionate share number of low-income patients with special needs to order to determiner whether these hospitals are entitled to receive [disproportionate share] payments.'"

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12. Hospital administrators express the costs of caring for a given patient population as a "diagnostic related group (DRG) weight." The trial court found that the average DRG weight of Medi-Cal patients treated by respondent hospitals was "much higher" than that of the Medi-Cal patients treated by in-state hospitals with which DHS has contracts. The court found, for example that the DRG weights of Medi-Cal patients treated at respondents Washoe Medical Center and Rogue Valley Medical Center are, respectively, 2.16 and 1.77, more than twice as high as the average DRG weight of contracting in-state hospitals, which is only .87.

B.

The still evolving jurisprudence of the dormant Commerce Clause traces the fitful efforts of the United States Supreme Court to establish a satisfactory theoretical basis for a doctrine that is not explicit in the text of the Constitution but may only be inferred.[13/] As is widely appreciated, not least of all by members of the United States Supreme Court, our high court has yet to provide a fully coherent theory of the negative dimension of the Commerce Clause that usefully assists application of the doctrine.[14/] (3) Under the Supreme Court's

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13. For a concise analysis of the theoretical problems presented by the doctrine of a dormant Commerce Clause, and the different approaches taken by the Supreme Court over time, see 1 Tribe, American Constitutional Law (3d ed. 2000) sections 6-2 through 6-6, pages 1029-1068.

14. Chief Justice Rehnquist has observed that "the jurisprudence of the 'negative side' of the Commerce Clause remains hopelessly confused." (*Kassel v. Consolidated Freightways Corp. of Delaware* (1981) 450 U.S. 662, 70 [101 S.Ct. 1309, 1334, 67 L.Ed.2d 580] (dis. opn. of Rehnquist, C.J.).) In an opinion joined in, by among others, Justice Ginsburg, Justice Scalia agreed that "[t]he Court's negative Commerce Clause jurisprudence has drifted far from its moorings," (*Camps Newfound/Owatonna, Inc. v. Town of Harrison* (1997) 520 U.S. 564, 595 [117 S.Ct. 1590, 1608, 137 L.Ed.2d 852] dis. opn. of Scalia, J.)), and Justice Thomas, who believes this "failed jurisprudence" is "overbroad and unnecessary," believes it ought to be "abandon[ed]." (*Camps Newfound/Owatonna, Inc. v. Town of Harrison, supra*, at p. 610 [117 S.Ct. at p. 1615] (dis. opn. of Thomas, J.) While the Supreme Court has "articulated a variety of tests in an attempt to describe the difference between those regulations that the Commerce Clause permits and those regulations that if prohibits" (*CTS Corp. v. Dynamics Corp. of American, supra*, 481 U.S. at p. 87 [107 S.Ct. at p. 1648]), it has provided little clear direction as to the hierarchy of values governing the course that must be taken when policies the various tests advance are in conflict. (See, e.g., Cushman, *Formalism and Realism in Commerce Clause Jurisprudence* (2000) 67 U. Chi. L.Rev. 1089.) Professor Tribe suggests, however, that though it is generally lamentable, the "doctrinal disarray" in this area has the virtue of

current approach, it appears that "a state law must, in the first instance, concern a legitimate state end. Second, even if they have a legitimate aim, state regulations that discriminate against interstate or out-of-state commerce are subject to rigorous scrutiny that approaches *per se* invalidity. Finally, even if a regulation does not discriminate against interstate commerce, it must be struck down if the burden imposes on interstate commerce is 'clearly excessive in relation to the putative local benefits.'" (1 Tribe, American Constitutional Law, *supra*, § 6-5, pp. 1050-1051, fns. omitted.) By discrimination, the Supreme Court means "differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter." (*Oregon Waste Systems, Inc. v. Department of Environmental Quality, supra*, 511 U.S. 93, 99 [114 S.Ct. 1345, 1350].)

(4a) DHS's reimbursement scheme obviously discriminates against out-of-state hospitals like respondents' that treat significant numbers of Medi-Cal patients. DHS's argument that the scheme is fair, boils down to no more than the false assertion that paying out-of-state hospitals the average of what DHS pays in-state hospitals with which it has contracts simply means that "out-of-state hospitals with which it has contracts simply means that "out-of-state hospitals will receive less than come California contract hospitals receive and more than others do." This superficial argument ignores findings and substantial evidence that the "cost-mix" of Medi-Cal patients

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permitting ad hoc reactions to particular cases that are sometimes warranted. "The plainly manipulable and at times anachronistically metaphysical character of [dormant Commerce Clause] doctrines and the dubious consistency of their complex exceptions suggest that the Supreme Court has preserved them with an eye to their discretionary application in order to prevent what appear to be instances of intolerable local or state interference with interstate markets." (1 Tribe, American Constitutional Law, *supra*, § 6-14, p. 1104.)

cared for by respondent hospitals is considerably higher than that of the in-state hospitals with which DHS contracts, so that the average rate paid such in-state hospitals in an invidious basis upon which to calculate the level of reimbursement that will fairly compensate respondents.

DHS also ignores the fact that the discrimination found by the trial court relates not just to the undercompensation of out-of-state hospitals, but the denial to them of administrative or judicial processes to challenge the adequacy of reimbursement, which are available to in-state hospitals. (5) As the trial court correctly noted, procedural distinctions providing greater rights to in-state than out-of-state interests have been held to impermissibly burden interstate commerce. *Bendix Autolite Corp. v. Midwesco Enterprises* (1988) 486 U.S. 888 [108 S.Ct. 2218, 100 L.Ed.2d 896] is illustrative. That case involved an Ohio law tolling the statute of limitations for any period that a person or corporation is not "present" in the state. To be present in Ohio, a foreign corporation must appoint an agent for service of process, which operates as consent to the general jurisdiction of Ohio courts. The Supreme Court found that the tolling provision— which "gave Ohio tort plaintiffs unlimited time to sue out-of-state (but not in-state) defendants" (Reynoldsville Casket Co. v. Hyde (1995) 514 U.S. 749, 750 [115 S.Ct. 1745, 1747, 131 L.Ed.2d 820])–violated the Commerce Clause. As the court explained, the Ohio statutory scheme "forces a foreign corporation to choose between exposure to the general jurisdiction of Ohio courts or forfeiture of the limitations defense, remaining subject to suit in Ohio in perpetuity. Requiring a foreign corporation to appoint an agent for service in all cases and to defend itself with reference to all transactions, including those in which it did not have the minimum contracts necessary for supporting personal jurisdiction, it is a significant burden." (*Bendix, supra*, at p. 893 [108 S.Ct. at p. 2221].)

(4b) The reimbursement scheme at issue here does not provide out-of-state hospitals the sort of Hobson's choice compelled in *Bendix,* or any choice at all; it simply deprives them of the procedural rights in-state hospitals possess to effectively challenge the adequacy of the compensation they receive for the service they provide. (*Goleta Valley Community Hospital v. Department of Health Services* (1983) 149 Cal.App.3d 1124 [197 Cal.Rptr. 294].)

While differences in the treatment of in-state and out-of-state hospitals that are demonstrably necessary would be constitutionally tolerable, the total indifference of DHS to the true cost of the care provided by out-of-state hospitals which serve significant numbers of Medi-Cal patients, and the denial to such hospitals of any effective way in which to seek and obtain the administrative and judicial relief made available to in-state hospitals, is facially untenable. It must be kept in mind that, for purposes of the dormant Commerce Clause, the Supreme Court has defined discrimination very expansively. **(6)** "Any disparity in the treatment of in-state and out-of-state interests-whether businesses, users, or products-constitutes discrimination, even if the disparity is slight. Moreover, the Court has declared that, 'where discrimination is patent, . . . neither a widespread advantage to in-state interests nor a widespread disadvantage to out-of-state competitors need be shown' in order to invalidate the law. Nor does a finding of 'discrimination' necessarily depend on economic analysis." (1 Tribe, American Constitutional Law, *supra* § 6-6, pp. 1059-1060, fns. omitted.)

(4c) In light of the profound judicial antipathy to state regulations that discriminate against out-of-state economic interests, DHS's scheme must be subjected to the most rigorous judicial scrutiny. As the United States Supreme Court has repeatedly declared: "where simple economic protectionism is effected by state legislation, a virtually *per se* rule of invalidity

has been erected." (*Philadelphia v. New Jersey* (1978) 437 U.S. 617, 624 [98 S.Ct. 2531, 2535, 57 L.Ed.2d 475]; accord, *Hughes v. Oklahoma* (1979) 441 U.S. 322,337 [99 S.Ct. 1727, 1737, 60 L.Ed.2d 250] ["facial discrimination by itself may be a fatal defect"]; *Sporhase v. Nebraska ex rel. Douglas* (1982) 458 U.S. 941, 958 [102 S.Ct. 3456, 2465, 73 L.Ed.2d 1254] ["facially discriminatory legislation" merited " 'strictest scrutiny' "]; *Chemical Waste Management, Inc. v. Hunt* (1992) 504 U.S. 334, 342 [112 S.Ct. 2009, 2014, 119 L.Ed.2d 121] ["Once a state tax is found to discriminate against out-of-state commerce, it is typically struck down without further inquiry."]; *Oregon Waste Systems, Inc. v. Department of Environmental Quality, supra,* 511 U.S. 93, 99 [114 S.Ct. 1345, 1350] ["If a restriction on commerce is discriminatory, it is virtually *per se* invalid."].) The California Supreme Court has of course been equally strict. Speaking for a unanimous court, Chief Justice George has observed that practices which discriminate against interstate commerce must be subjected to "heightened scrutiny." *(Woosley v. State of California* (1992) 3 Cal.4th 758, 783 [13 Cal.Rptr.2d 30, 828 P.2d 758].) Our High court has also refused to indulge discrimination on the ground of "the legitimacy of the state interests that the statute is designed to protect, the degree and scope of the discrimination, and the volume of commerce affected." *(Pacific Merchant Shipping Assn. v. Voss* (1995) 12 Cal.4th 503, 517 [48 Cal.Rptr.2d 582, 907 P.2d 430].) The discrimination prohibited by the dormant Commerce Clause is simply *any* " 'differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter.' " *(Ibid.)*

(7) Facially discriminatory state regulations of the sort presented in this case must be stricken "unless the discrimination is demonstrably justified by a valid factor unrelated to economic protectionism." *(New Energy Co. of Indiana v. Limbach, supra,* 486 U.S. 269, 274 [108 S.Ct. 1803, 1808.].) **(4d)** DHS's defense to respondents' Commerce Clause

claim does not genuinely rest on any such justification.[15] Its chief defense lies instead in the unusual contention that its reimbursement scheme cannot offend the Commerce Clause because it does not relate to an article of commerce.

Allowing that there is an interstate aspect to this case, DHS insists that, unlike the Commerce Clause cases relied upon by respondents and by the trial court, in which there was competition between the in-state and out -of-state enterprises whose economic interests were at stake,[16] there is no competition between in-state and out-of-state hospitals relating to the treatment of Medi-Cal patients and the challenged regulation therefore does not affect the flow of commerce. DHS emphasizes that respondent hospitals do not send their doctors into California to do business, but simply provide treatment in their states to California residents who happen to be there.

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15. The only justification DHS offers for the disparate compensation of in-state and out-of-state hospitals is that it is impossible, as a practical matter, to enter into a cost sensitive contract with "every hospital across the nation," most of which are distant and rarely treat Med-Cal patients. However, DHS does not explain why it cannot either contract with the relatively few large hospitals in nearby regions of adjacent states that treat significant numbers of such patients (if they are willing to make their cost figures available and submit to audits), or voluntarily comply with federally approved procedures for reimbursing out-off-state hospitals that require the reasonable costs of such hospitals to be taken into account, which the trial court ordered DHS to comply with. Nor has DHS offered any explanation why large out-of-state hospitals that treat significant numbers of Medi-Cal patients and are willing to submit tot the authority of DHS and the jurisdiction of California court cannot be allowed administrative and judicial processes to challenge the adequacy of the compensation they receive.

16. *Oregon Waste Systems, Inc. v. Department of Environmental Quality, supra,* 511 U.S. 93; *Chemical Waste Management, Inc. v. Hunt, supra,* 504 U.S. 334; *Philadelphia v. New Jersey, supra,* 437 U.S. 617; *Hunt v. Washington Apple Advertising Comm'n* (1977) 432 U.S. 333 [97 S.Ct. 2434, 53 L.Ed.2d 383].

According to DHS, when respondents provide such care and are paid by California, "there is no competitive consequence. California hospitals do not achieve an advantage over [respondent hospitals] as a consequence of the latter's being paid less than some California hospitals might be paid for the same services." DHS also emphasizes that, because hospitals have a legal obligation to provide services to persons whose health care is subsidized under the Medicare program, treatment decisions are not made on the basis of competitive considerations. For this reason, DHS argues, "all hospitals in all states are on an equal footing. They all must treat out-of-state residents. Some may receive more money than others but there is no law which requires parity or any uniform payment system and, in any event, differing reimbursement rates have no effect on the hospitals' statutory obligation to render treatment." We are not impressed with this argument.

To begin with, the Supreme Court's definition of interstate commerce is notably capacious. **(8)** "All objects of interstate trade merit Commerce Clause protection; none is excluded by definition at the outset." *(Philadelphia v. New Jersey, supra,* 437 U.S. at p. 622 [98 S.Ct. at p. 2534].) The provision of services to residents of other states is no less an object of interstate commerce than the sale of goods. (See, e.g., *Camps Newfound/Owatonna, Inc. v. Town of Harrison, supra,* 520 U.S. 564.)

(4e) The flaw in DHS's argument lies in the artificiality of its definition of the commerce at issue in this case. It is true that, unlike most other services that are offered for a fee, the service of treating Medi-Cal patients (which the recipient of care cannot afford and the government does not fully subsidize) is by its very nature unprofitable, and hospitals therefore have no incentive to compete for such patients. However, while there is no competition between in-state and out-of-state hospitals for Medi-Cal patients, beneficiaries of the Medi-Cal program are

not the only Californians who may obtain needed medical assistance from out-of-state hospitals, particularly those located in nearby communities in adjacent state. Respondents and undoubtedly other out-of-state hospitals located close to our state line serve not just Medi-Cal patients but many other California residents in need of care who are able to pay their own way or whose health insurance more fully compensates health care providers. With respect to this universe of patients there is competition between and among in-state and out-of-state hospitals located in the same region. Respondents' Commerce Clause claim is built on the theory that the undercompensation they receive from DHS regarding a class of patients they cannot legally refuse to serve places them at a disadvantage against nearby in-state hospitals with which they compete for profitable business. The only way out-of-state hospitals can recover the inordinately high unreimbursed costs they incur by treating Medi-Cal patients is either to charge other patients more than the California hospitals with which they compete need to charge in order to cover their costs or to accept lower profit margins than the in-state competitors they have relieved of the need to serve unprofitable Medi-Cal patients. Without ever explicitly addressing the issue, DHS untenably assumes California hospitals do not compete with out-of-state hospitals for other patients, and ignores the manner in which its reimbursement scheme places out-of-state hospitals at a disadvantage with respect to that competition. In short, the article of commerce with which we are here concerned is not the provision of hospital care to Medi-Cal patients, as DHS maintains, but the provision of such care to *all* persons to whom a hospital can make it available. The evidence supports the trial court determination that DHS's reimbursement scheme adversely affected respondents' overall commercial health, to the advantage of the in-state hospitals with which they compete, and it is in that way that the scheme burdens the interstate flow of the commercial services respondents provide.

We are not persuaded by DHS's contention that the revenues out-of-state hospitals receive from treating Medi-Cal patients are such a small portion of their total revenues that the undercompensation they receive for this service does not materially affect their ability to compete with in-state hospitals. Even if Medi-Cal patients provide a small portion of the revenues of respondent hospitals, it must be remembered that even a slight disparity in the treatment of in-state and out-of-state interests may offend the dormant Commerce Clause. For example, in *Oregon Waste Systems, Inc. v. Department of Environmental Quality, supra,* 511 U/Ss/ 93, the Supreme Court found that a $2.25 per ton surcharge on out-of-state waste impermissibly burdened interstate commerce even though it amounted to an increase of only 14 cents per week for the average user. The court stated that its precedents "clearly establish that the degree of a differential burden or charge on interstate commerce 'measures only the *extent* of the discrimination' and 'is of no relevance to the determination whether a State has discriminated against interstate commerce.' " *(Id.* at p. 100, fn. 4 [114 S.Ct. at p. 1350], original italics, quoting *Wyoming v. Oklahoma* (1992) 502 U.S. 437, 455 [112 S.Ct. 789, 801 117 L.Ed.2d 1].)

DHS argues, finally, that even if its reimbursement scheme burdens interstate commerce, the so-called "market participation exception" exempts its conduct from prohibitions of the dormant Commerce Clause that might otherwise apply. We disagree.

(9) As the Supreme Court has explained, "[n]othing in the purposes animating the Commerce Clause prohibits a State, in the absence of congressional action, from participating in the market and exercising the right to favor its own citizens over others." *(Hughes v. Alexandria Scrap Corp.* (1976) 426 U.S. 794, 810 [96 S.Ct. 2488, 2498, 49 L.Ed.2d 220].) Thus, "if a State is acting as a market participant, rather than as a market

regulator, the dormant Commerce Clause places no limitation on its activities" *(South-Central Timber Dev. v. Wunnicke* (1984) 467 U.S. 82, 93 [104 S.Ct. 2237, 2243, 81 L.Ed.2d 71]; accord, *Wyoming v. Oklahoma, supra,* 502, U.S. 437, 458 [112 S.Ct. 789, 802]; *Reeves, Inc. v. Stake* (1980) 447 U.S. 429, 439 [100 S.Ct. 2271, 2278-2279, 65 L.Ed.2d 244]. Application of this principle invariably turns upon whether the state conduct at issue truly constitutes participation in an open private market or is instead simply a form of governmental regulation. "When a state engages in market 'participation' - that is, when it enters the open market as a buyer or seller on the same footing as private parties-there is less danger that the state's activity will interfere with Congress's plenary power to regulate the market. As the Court has explained, the Commerce Clause 'restricts "state taxes and regulatory measures impeding free private trade in the national marketplace," but "[there] is no indication of a constitutional plan to limit the ability of the States themselves to operate freely in the free market." ' [Citations.} Pursuant to this doctrine-the 'market participant' exception to the dormant Commerce Clause-sates are permitted to enter a market with the same freedoms and subject to the same restrictions as a private party. To the extent that a state is acting as a market participant it may pick and choose its business partners, its terms of doing business, and its business goals-jus as if it were a private party." *(SSC Corp. v. Town of Smithtown* (2d Cir. 1995) 66 F.3d 502, 510, fn. omitted.)

(4f) DHS claims the market participation exception applies because the State of California "participates in the purchase of medical services for those of its residents who require acute inpatient care when out-of-state." The defects in this argument are readily apparent. First, the state is not itself a consumer of the service in question, nor does it pick and choose service providers. Discharging conventional regulatory responsibilities imposed on it by state and federal law, the state, through DHS, merely reimburses those service providers

selected by Medi-Cal recipients in need of medical care. The level of reimbursement DHS allows is clearly not responsive to market forces. Moreover, as DHS itself correctly points out in a different connection, There is no genuine private market regarding the delivery of care to Medi-Cal patients in which the state could participate. Though the treatment of Medi-Cal patients is less costly for in-state than out-of-state hospitals, it is in both cases inherently unprofitable; hospitals serve Medi-Cal patients only because they cannot legally refuse to do so. In sum, when it determines the level of compensation hospitals are entitled to receive for the treatment of Medi-Call patients, DHS is not participating in an open market but simply carrying out a traditional state regulatory responsibility. The market participation exception therefore does not apply.

The trial court finding that DHS's discriminatory reimbursement scheme came within the negative sweep of the Commerce Clause was correct.

III.

The Equal Protection Clause.

The equal protection clause (Equal Protection Clause) of the Fourteenth Amendment commands that no state shall "deny to any person within its jurisdiction the equal protection of the laws." (U.S. Const., 14th Amend., § 1.) The provisions of the California Constitution guaranteeing equal protection, set forth in article I, section 7, are "substantially the equivalent of the equal protection clause of the Fourteenth Amendment . . . ." *(Department of Mental Hygiene v. Kirchner* (1965) 62 Cal.2d 586, 588 [43 Cal.Rptr. 329, 400 P.2d 321].)

(10) Where, as here, the differential treatment of in-state and out-of-state enterprises does not relate to any fundamental interests, such as the right to vote, or suspect classifications,

such as race or sexual orientation, the question is whether there is a rational basis for the different treatment. " '[W]hatever the extent of a State's authority to exclude foreign corporations from doing business within its boundaries, that authority does not justify imposition of more onerous taxes or other burdens on foreign corporations than those imposed on domestic corporations, unless the discrimination between foreign and domestic corporations bears a rational relation to a legitimate state purpose.' " *(Metropolitan Life Ins. Co. v. Ward* (1985) 470 U.S. 869, 875 [105 S.Ct. 1676, 1680, 84 L.Ed.2d 751].)

(11) Discriminatory state conduct that violates the Commerce Clause does not necessarily offend the Equal Protection Clause. *(Bendix Autolite Corp. V. Midwesco Enterprises, Inc. supra,* 486 U.S. 888, 894 [108 S.Ct. 2218, 2222].) **(12)** Moreover, as the seminal opinion of *Dandridge v. Williams* (1970) 397 U.S. 471 [90 S.Ct. 1153, 25 L.Ed.2d 491] makes clear, "[i]n the area of economics and social welfare, a State does not violate the Equal Protection Clause merely because the classifications made by its laws are imperfect. If the classification has some 'reasonable basis,' it does not offend the Constitution simply because the classification 'is not made with mathematical nicety or because in practice it results in some inequality.' [Citation.] 'The problems of government are practical ones and may justify, if they do not require, rough accommodations-illogical it may be, and unscientific.' [Citation.] 'A statutory discrimination will not be set aside if any state of facts reasonably may be conceived to justify it.' [Citation.]" *(Id.* at p. 485 [~~90 S.Ct.~~ at p. 1161]; *Hansen v. City of Buenaventura* (1986) 42 Cal.3d 1172, 1190 (233 Cal.Rptr. 22, 729 P.2d 186.])

(13) After observing that DHS failed to present any such governmental interest, and that "budgetary interests" would not suffice (citing *AMISUB (PSL), Inc. v. Colorado Dept. of Social Services* (10th Cir. 1989) 879 F.2d 789, 800-801, cert. den. 496

U.S. 935 [110 S.Ct. 3212, 110 L.Ed.2d 660]; *Tallahassee Memorial Regional Medical Center v. Cook* (11th Cir. 1997) 109 F.3d 693, 704), the trial court found that DHS's differential treatment of in-state and out-of-state hospitals bore no rational relationship to any legitimate state purpose.

DHS contests this ruling not just by renewing its contention that its reimbursement scheme is fair and rational, but also by claiming that, as a practical matter, there is no workable alternative. Respondents point out that the argument that basing their reimbursement on the average rate paid in-state hospitals with which DHS has contracts (as prescribed by subdivision (i)) is fair and rational cannot be squared with the determinations of the federal district court that DHS "gathered no information on the costs incurred by out-of-state hospitals and performed no empirical analysis of the effects of the reimbursement scheme on out-of-state hospitals," and claim DHS is therefore collaterally estopped from arguing that the scheme is reasonable. (Italics omitted.) We feel it unnecessary to decide the extent to which DHS may be collaterally estopped from defending its scheme because the trial court independently addressed the defense and found it wanting, as we have. Moreover, DHS's claim that its scheme is rational because no workable alternative exists appears never to have been raised in the federal proceedings.

DHS sums up this argument in its opening brief as follows: "By definition, [out-of-state hospitals] are outside the borders of this state and, in most instances, quite distant. They are not subject to California jurisdiction; they are beyond the control of the California Legislature and the reach of regulations enacted by DHS. Moreover, the vast majority of them treat California residents only on an episodic basis. Whereas . . . the state can contract with in-state hospitals to treat California residents, the state can hardly contract with the 7500 hospitals across the nation which conceivably would have occasion to

treat a California resident. And whereas the non-contract hospitals in California submit annual cost data to the state, are subjected to peer grouping, quality of care review, review of staffing levels, and state audits, manifestly these procedures cannot be applied to hospitals across the country. [¶] Thus, it is clear that out-of-state hospitals cannot be paid based on the methodologies used to pay California hospitals."

It is quite true that "where a group possesses 'distinguishing characteristics relevant to interests the State has the authority to implement,' a State's decision to act on the basis of those differences does not give rise to a constitutional violation." (*Board of Trustees of Univ. of Ala. v. Garrett* (2001) 531 U.S. 356, 366-367 [121 S.Ct. 955, 963, 148 L.Ed.2d 866].) However, the characteristics of the "7500 hospitals across the nation which conceivably would have occasion to treat California residents" that DHS emphasizes most heavily are not attributable to respondents and other similarly situated out-of-state hospitals. As earlier explained, respondent hospitals are each located in areas of adjacent sates easily accessible to many California residents. The Californians they serve include not just a few travelers who appear on an episodic basis but significant numbers of Medi-Cal beneficiaries residing in the far northern and eastern reaches of our state, which do not possess many large medical facilities able to provide the high level of intensive care that can be obtained from respondents' facilities, which are relatively close. As the trial court found, respondents "provide the full medical services needed for acute care Medi-Cal patients not just visiting the states of Arizona, Oregon or Nevada, but also those Californians who must avail themselves of [respondents'] facilities . . . because they are the closest major trauma centers *available to Medi-Cal participants residing in California.*" (Original italics.)

DHS's argument that there is no workable alternative to the reimbursement scheme it began using in 1992 consists of little

more than an explanation of the practical impossibility of treating out-of-state hospitals in exactly the same manner as in-state hospitals. The argument posits a straw man. Respondents have never proposed that they be treated in exactly the same manner as in-state hospitals. All they sought, and all the trial court ordered, was that DHS revert to the reimbursement scheme prescribed by DHS regulations in effect prior to the enactment of subdivision (i) in 1992 (tit. 22, former § 51543 (1992)), which had been approved by the HCFA and which DHS employed for many years without complaint.[17/] The prior regulation allowed for five different reimbursement methodologies, depending upon the availability of specified information. The trial court found respondents presented adequate data supporting use of the first methodology set forth in the regulation, which provided for compensating an out-of-state hospital "a percentage of allowable billed charges" based on "[t]he average percentage of charges, up to a maximum of 100 percent, which is paid to the hospital by that hospital's state." (*Id.*, former § 51543, subdiv. (a)(1).) Neither in the trial court nor in this court has DHS shown that use of the reimbursement scheme it previously employed would be unduly burdensome in any way or unfair to the State of California.

DHS has failed to demonstrate that its differential treatment of respondent hospitals on the basis of their location out of state is rationally related to a legitimate governmental purpose. Its conduct therefore infringes respondents' rights

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17. Use of the prior reimbursement regulations was sought by respondents and ordered by the court on the basis of federal case law indicating that invalidation of a current state scheme for the reimbursement of Mediaid providers triggers imposition of a prior federally approved scheme. (*Exeter Memorial Hosp. Ass'n v. Belshe* (E.D.Cal. 1996) 943 F. Supp. 1239, 1242; see also *Mass. Fed. of Nursing Homes v. Com. of Mass* (D.Mass. 1992) 791 F.Supp. 899, 905; *Pinnacle Nursing Home v. Axelrod, supra* 719 F.Supp. 1173, 1182-1183.)

under the equal protection clauses of the state and federal Constitutions.

IV.

Respondents Are Entitled to Prejudgment Interest but Only at the Rate of 7 Percent.

Section 3287, subdivision (a), of the Civil Code states in material part: "Every person who is entitled to recover damages *certain, or capable of being made certain by calculation*, and the right to recover which is vested in him upon a particular day, is entitled also to recover interest thereon from that day, except during such time as the debtor is prevented by law, or the act of the creditor from paying the debt . . . ." (Italics added.)

(14a) DHS contends the award of prejudgment interest was improper because the damages to which respondents were entitled were never certain or capable of being made certain. It argues that the uncertainty of the amount of damages respondents had a right to recover is shown not only by the fact that respondents presented different damage models from which they asked the court to choose, but also by the disparity between the amount of damages sought ("$20 million or according to proof") and that awarded. In reply to this argument, respondents rely upon cases in which plaintiffs were awarded prejudgment interest even though they had proposed different measures of damages. (*Shell Oil Co. v. National Union Fire Ins. Co.* (1996) 44 Cal.App.4th 1633 [52 Cal.Rptr.2d 580] (*Shell Oil Co.*); *Fireman's Fund Ins. Co. v. Allstate Ins. Co.* (1991) 234 Cal.App.3d 1154 [286 Cal.Rptr. 146].)

In *Shell Oil Co., supra,* 44 Cal.App.4th 1633 the plaintiff oil company was awarded damages for breach of a liability insurance policy. The trial court, sitting without a jury, found that the defendant insurance company, National, had provided

coverage for an accident that resulted from Shell's sole negligence, and that National did not fully discharge its contractual duties by paying its policy limit in settlement for a coinsured, and awarded Shell prejudgment interest on the $500,000 damages it received for National's breach of coverage duties. The Court of Appeal affirmed the trial court in all respects. As to prejudgment interest, the appellate court acknowledged Shell had advanced alternative theories of liability, but pointed out that the "alternative theories required only the court's legal determination of which was appropriate; the amount of damages would thereby be fixed." (*Shell Oil Co., supra,* at p. 1651.) The court observed that the situation was comparable to that in *Hartford Accident & Indemnity Co. v. Sequoia Ins. Co.* (1989) 211 Cal.App.3d 1285 [260 Cal.Rptr. 190], "in which the overall responsibility of an insurer was in dispute, and the amount recoverable from it depended on how the court assigned priorities among it and two other insurers. There, as here, 'the amount of damages under either formula was readily ascertainable by mathematical calculation' (*id.* at p. 1307), and prejudgment interest was appropriate." (*Shell Oil Co., supra,* 44 Cal.App.4th at p. 1651.) *Fireman's Fund Ins. Co. v. Allstate Ins. Co., supra,* 234 Cal.App.3d 1154 also involved a situation in which the prevailing party advanced alternative theories of liability. Affirming an award of prejudgment interest, the Court of Appeal observed that "[w]hatever uncertainty about the extent of Fireman's liability may have been fostered by the alternative theories Fireman's proposed, we do not view that uncertainty as an impediment to the award of prejudgment interest. While Fireman's proposed a general formula based on four inapt theories of lesser liability, it also suggested a specific amount due Allstate and Northbrook under each theory. Through it all, the extent of Fireman's exposure remained purely a question of law. Thus, the amounts proposed under Fireman's theories or the amounts legally compelled by section 3634 were readily ascertainable." (*Id.* at p. 1174, italics omitted.)

In the present case, like the three just briefly described, respondents' alternative theories as to the manner in which damages should be calculated were all tethered to legal theories. Although the complaint did pray for damages of $20 million or according to proof," respondents made it clear long before trial, at the time they sought summary judgment, that they sought a specific amount of damages and that it was the product of applying a specific government-approved formula. As noted, the method of calculating damages respondents advanced, and the one adopted by the trial court, was retroactive application of the reimbursement methodology approved by HCFA and used by DHS prior to the 1992 enactment of subdivision (i). This contention was based on law, not disputed evidence. Respondents emphasized that federal courts consistently mandated retroactive reimbursement pursuant to a previous HCFA approved state reimbursement methodology after invalidating a current scheme (*Exeter Memorial Hospital Ass'n v. Belshe, supra,* 943 F.Supp. 1239, 1242, affd. (1998) 145 F.3d 1106; *Pinnacle Nursing Home v. Axelrod, supra,* 719 F.Supp. 1173, revd. in part on other grounds, 928 F.2d 1306; *Mass. Fed. of Nursing Homes v. Com. of Mass., supra,* 791 F.Supp. 899), and vigorously urged the trial court to follow suit. It was only in the event (which did not materialize) that the court decided that the previous HCFA approved reimbursement scheme should *not* be judicially imposed that respondents urged they should at least be provided a right to seek administrative adjustments of prior reimbursements pursuant to a regulation permitting such adjustments (tit.22, § 51543, subd. (b) which out-of-state hospitals had been prevented from suing by the enactment of subdivision (i), which did not allow for adjustments. Respondents never proposed a specific amount of damages they felt they were entitled to recover in this manner. If this route to recovery had been available, respondents presumably would have sought adjustments based on the same HCFA-approved formula they persuaded the trial court to adopt.

The only other theory of recovery respondents advanced was in connection with their quantum meruit claim, which sought an amount *over and above* that to which they claimed entitlement under the previous reimbursement scheme approved by HCFA. Under this legal theory, respondents sought to recover *all* of the costs they actually incurred, the amount of which was never factually disputed, minus the amounts DHS had paid, which was also undisputed. The trial court rejected this claim because it did not feel respondents were as a matter of law entitled to reimbursement of all of the costs incurred in the treatment of Med-Cal patients.

(15) "'The test for recovery of prejudgment interest under [Civil Code] section 3287, subdivision (a) is whether *defendant* actually know[s] the amount owed or from reasonably available information could the defendant have computed that amount. [Citation.]' (*Cassinos v. Union Oil Co.* [(1993)] 14 Cal.App.4th [1770,] 1789 [18 Cal.Rptr.2d 574], original italics; *Hartford Accident & Indemnity Co. v. Sequoia Ins. Co.* (1989) 211 Cal.App.3d 1285, 1307 [260 Cal.Rptr. 190]; *Chesapeake Industries, Inc. v. Togova Enterprises, Inc.* (1983) 149 Cal.App.3d 901, 907 [197 Cal.Rptr. 348].) 'The statute . . . does not authorize prejudgment interest where the amount of damage, as opposed to the determination of liability, "depends upon a judicial determination based upon conflicting evidence and it is not ascertainable from truthful data supplied by the claimant to his debtor." [Citations.]' (*Fireman's Fund Insurance Co. v. Allstate Ins. Co., [supra,]* 234 Cal.App.3d 1154, 1173. . . .) Thus, where the amount of damages cannot be resolved except by verdict or judgment, prejudgment interest is not appropriate. (*Stein v. Southern Cal. Edison Co.* [(1992)] 7 Cal.App.4th [565,] 573 [8 Cal.Rptr.2d 907].)" (*Wisper Corp. v. California Commerce Bank* (1996) 49 Cal.App.4th 948, 960 [57 Cal.Rptr.2d 141].)

(14b) Applying the foregoing principles to the facts

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before us, it is clear the amount of damages owed respondent hospitals by DHS was sufficiently calculable prior to trial. In reality, respondents put forth only two methods of calculating damages. The proposed methods did not conflict, because use of the second (quantum meruit) would only have augmented the amount produced by the first (the previous HCFA-approved methodology), and neither method required reliance on disputed cost figures. The damages calculated by the court using the previous HCFA-approved methodology could have been computed by DHS from the same information used by the court, which was available to DHS at all material times. In short, the requirement that the damages be "certain" or "capable of being made certain . . . . " (Civ. Code, § 3287) in order for prejudgment interest to be awarded was satisfied in this case.

However, while the award of prejudgment interest was proper, the 10 percent rate of interest set by the court was excessive. The court appears to have fixed the rate of interest at 10 percent on the basis of subdivision (b) of Civil Code section 3289, which as material provides that "[i]f a contract entered into after January 1, 1986, does not stipulate a legal rate of interest, the obligation shall bear interest at a rate of 10 percent per annum after a breach." Respondent hospitals agree that, as their right to reimbursement from DHS is not based on contract, the rate of prejudgment interest should be that fixed by article XV, section 1 of the California Constitution; namely 7 percent per annum.

V.

Respondents Are Entitled to the Attorney Fees Awarded by the Court.

In its order directing the payment of damages and prejudgment interest, the court also declared that respondents "are entitled to an award of attorneys fees pursuant to the

private attorney general doctrine [(Code Civ. Proc., § 1021.5)], in the amount to be determined according to proof." In addition to their costs of $34, 620, respondents sought an award of attorney fees in the amount of $1,270,967, which necessitated application of a 1.5 multiplier to a proposed lodestar figure of $859,977.79. In an order filed on March 29, 2001, the trial court found that respondents were entitled to attorney fees under the private attorney general theory codified in Code of Civil Procedure section 1021.5 (section 1021.5). After finding that $380 per hour was a reasonable rate, and deducting 86.40 hours from the 2,223.30 hours submitted by respondents' counsel, the trial court set a lodestar amount of $827,145.79. The court refused to enhance this figure with a multiplier because it concluded that the lodestar amount was sufficient. Approximately one-third of the hours compensated by the award were devoted to the related federal proceedings.

On appeal DHS argues that (1) respondents are not entitled to any attorney fees because they cannot satisfy the requisites of section 1021.5; but even if they are deemed to have satisfied the statute, (2) they are not entitled to fees incurred in the federal proceedings; and (3) the hourly rates allowed by the trial court are excessive, as are the amount of hours for which respondents were compensated. We believe DHS waived objection to the trial court's determination that respondents were entitled to an award of attorney fees under section 1021.5, and that it may on this appeal challenge only the amount of fees awarded.

A.

In its order of December 14, 2000, the trial court stated its intention to award fees pursuant to the private attorney general theory codified in section 1021.5. Accordingly, the last sentence of the judgment, which issued on December 20, 2000, stated that "the Plaintiff Hospitals are entitled to an award of attorneys fees pursuant to the private attorney general doctrine

and costs, in amounts to be determined according to proof." Respondents served DHS with written notice of entry of judgment on December 28, 2000. On February 14, 2001, at the hearing on attorney fees, counsel for respondents pointed out to the court that if DHS believed the court had used an incorrect or erroneous basis in determining that respondents were entitled to an attorney fee award, its remedy was to file a motion under Code of Civil Procedures section 663. Because DHS never filed such a motion, which was required by Code of Civil Procedure section 663a to be filed within 15 days of service of written notice of entry of judgment, respondents maintained it was too late do to so. The trial court agreed. Its order dated March 29, 2001, setting the amount of attorney fees states that DHS had until January 12, 2001 to move to vacate the decision to award fees but did not oppose the award until February 2, 2001. Declaring that "[r]elief cannot be granted for the failure to take a jurisdictional step, such as the filing of a timely motion to vacate," the court concluded that "the defendants are jurisdictionally barred from challenging the Court's award of attorneys' fees."

(16) On appeal, in a supplemental letter brief requested by this court, DHS takes the position that the trial court's declaration that respondents were entitled to attorney fees was made prior to the time respondents filed their formal written motion for fees and that an award under section 1021.5 may only be made "upon motion," citing *Hospital Systems Inc. v. Office of Statewide Health etc. Development* (1994) 25 Cal.App.4th 1686, 1691 [30 Cal.Rptr.2d 922]. According to DHS, the inclusion of an attorney fee award in the judgment was therefore "beyond the court's jurisdiction."

DHS has "doubly waived" the right to present this argument on appeal. (*Campos v. Anderson* (1997) 57 Cal.App.4th 784, 794 [67 Cal.Rptr.2d 350].) First, the theory was never presented to the trial court, either in a motion to

vacate pursuant to Code of Civil Procedure section 663, in the memorandum in opposition to the award of attorney fees DHS submitted to the trial court, orally at the postjudgment hearing conducted by the court on the issue of fees, or in any other way. Had it been presented, and had the court agreed, the problem could easily have been rectified, which may be the reason the argument was never raised. "An appellate court will not consider procedural defects or erroneous rulings where an objection could have been, but was not, raised in the court below." *(Steven W. v. Matthew S.* (1995) 33 Cal.App.4th 1108, 1117 [39 Cal.Rptr.2d 535].) It is unfair to the trial judge and to the adverse party to take advantage of an alleged error on appeal where it could easily have been corrected at trial. *(Doers v. Golden Gate Bridge etc. Dist.* (1979) 23 Cal.3d 180, 184, fn. 1 [151 Cal.Rptr. 837, 588 P.2d 1261]; accord, *Planned Protective Services, Inc. v. Gorton* (1988) 200 Cal.App.3d 1, 12-13 [245 Cal.Rptr, 790] [applying the rule in an appeal from the recovery of attorney fees].)

Furthermore, the issue was never raised in the opening and reply briefs DHS filed in this court. Points raised for the first time in a reply brief ordinarily need not be considered *(Heiner v. Kmart Corp.* (2000) 84 Cal.App.4th 335, 351 [100 Cal.Rptr.2d 854]; *Shade Foods, Inc. v. Innovative Products Sales & Marketing, Inc.* (2000) 78 Cal.App.4th 847, 894, fn. 10 [93 Cal.Rptr.2d 364), and such abstention is even more appropriate where, as here, the issue is not even mentioned in the reply brief but only in a supplemental postbriefing submission requested by the court. (*San Mateo Country Coastal Landowners' Assn. v. Country of San Mateo* (1995) 38 Cal.App.4th 523, 559,fn. 28 [45 Cal.Rptr.2d 117].)

DHS' s claim that the amount of fees awarded is excessive–because the hourly rates allowed were excessive and fees incurred in the federal proceedings should not have been allowed-are cognizable on appeal, however, as the amount was

not set forth in the judgment but in a postjudgment order that issued after briefing and oral argument, and this matter was raised by DHS at trial and its opening brief in this court.

B.

(17) With respect to the *amount* of fees awarded, there is no question our review must be highly deferential to the views of the trial court. *(Press v. Lucky Stores, Inc.* (1983) 34 Cal.3d 311, 321-322 [193 Ca;.Rptr. 900, 667 P.2d 704].) As our high court has repeatedly stated, " ' " [t]he "experienced trial judge is the best judge of the value of professional services rendered in his [or her] court, and while his judgment is of course subject to review, it will not be disturbed unless the appellate court is convinced that it is clearly wrong' --meaning that it abused its discretion." ' " *(Thayer v. Wells Fargo Bank N.A.* (2001) 92 Cal.App.4th 819, 832 [112 Cal.Rptr.2d 284], quoting *PLCM Group v. Dexter* (2000) 22 Cal.4th 1084, 1095 [95 Cal.Rptr.2d 198,997 P.2d 511], quoting *Serrano v. Priest* (1977) 20 Cal.3d 25, 49 [141 Cal.Rptr. 315, 569 P.2d 1303] and citing *Fed-Mart Corp. v. Pell Enterprises, Inc.* (1980) 111 Cal.App.3d 215, 228 [168 Cal.Rptr. 525] [an appellate court will interfere with a determination of reasonable attorney fees "only where there has been a manifest abuse of discretion"].)

1.

(18) DHS's contention that the amount of fees awarded was excessive consists in part of the claim that respondents were not entitled to compensation for time spent by their counsel on the federal case. According to DHS, respondents' victory in this case "in no way hinged on the federal action." DHS's plangent assertions that the federal rulings "have absolutely no significance" to the present litigation are unacceptable. To be sure, the dispositive federal rulings that DHS violated the Medicaid Act collaterally estopped DHS from

relitigating that precise issue in state court, but it does not follow that the statutory violations found by the federal courts are unrelated to the constitutional questions litigated in this action. As earlier explained, the trial court's conclusion that DHS's reimbursement scheme offended the dormant Commerce Clause rested in part on Judge Patel's determinations, affirmed by the Ninth Circuit, that DHS violated the Medicaid Act by gathering no information on the costs incurred by out-of-state hospitals, performing no empirical analysis of the effects of its reimbursement scheme on out-of-state hospitals, and failing to provide any other basis for a principled analysis as to whether its reimbursement of such hospitals was reasonable and adequate. The trial court also relied on Judge Patel's finding that DHS made no disproportionate share adjustment payments to out-of-state hospitals nor undertook an inquiry as to whether they were entitled to such payments. If the federal courts had not previously determined that DHS treatment of out-of-state hospitals did not comply with the federal statutory scheme the superior court would almost certainly have had to address that complex question, as DHS would surely have answered respondents' constitutional claims by arguing that the challenged conduct was fully consistent with the mandate of Congress.

DHS's argument that fees may be awarded for ancillary proceedings only if they are *necessary* to the action in which fees are sought is not unequivocally supported by the cases on which it relies. The pertinent case law relates primarily to cases involving administrative proceedings ancillary to a judicial action. In *Webb v. Dyer County Bd. of Ed.* (1985) 471 U.S. 234 [105 S.Ct. 1923, 85 L.Ed.2d 233], the federal district court decided that a Black schoolteacher, who prevailed in his section 1983 action (42 U.S.C. § 1983) challenging termination of his employment, was not entitled to attorney fees under the Civil Rights Attorney's Fees Awards Act of 1976 for time spent by counsel in the school board, although the teacher contended he

was entitled to fees on the basis that time spent by counsel in the school board proceedings was reasonably expended in preparation for the successful court action. The Supreme Court affirmed. Noting that the federal statute authorizing fees (42 U.S.C. § 1988) only authorized fees in an "action or proceeding to enforce [section 1983]," and gave the trial court discretion whether to award fees to a prevailing party, the court observed that "[a]dministrative proceedings established to enforce tenure rights created by state law simply are not any part of the proceedings to enforce § 1983, and even though the petitioner obtained relief from his dismissal in the later civil rights action, he is not *automatically* entitled to claim attorney's fees for time spent in the administrative process . . . ." (*Id.* at p. 241 [105 S.Ct. at p. 1927], italics added, fn. omitted.) Emphasizing that, as held in *Hensley v. Eckerhart* (1983) 461 U.S. 424 [103 S.Ct. 1933, 76 L.Ed.2d 40], the amount to be awarded necessarily depends "on the facts of each case" (*id.* at p. 429 [103 S.Ct. at p. 1937]), and that "the exercise of discretion by the district court must be respected" *(Webb*, at p. 242 [105 S.Ct. at p. 1928]), the court reiterated that "the most 'useful starting point for determining the amount of a reasonable fee is the number of hours expended on the litigation multiplied by a reasonable hourly rate.' " (*Ibid.*, quoting *Hensley, supra,* at p. 433 [103 S.Ct. at p. 1939].)

The question in *Webb* was "whether the time spent on the administrative work during the years before August 1979 [when the judicial action was commenced] should be included in its entirety or excluded in its entirety." *(Webb v. Dyer County Bd. of Ed., supra,* 471 U.S. at p. 243 [105 S.Ct. at p. 1929].) While the Supreme Court concluded that, on the record presented, the district court correctly held that all of the administrative work was not compensable, the court felt it necessary to " 'reemphasize that the district court has discretion in determining the amount of fee award.' [Citation.] When such an award is appealed, the reviewing court must evaluate its reasonableness

with appropriate deference." *(Id.* at p.244 [105 S.Ct. at p. 1929], fn. omitted.) The Supreme Court clearly never intended to foreclose a fee award that compensates a prevailing party for work performed in administrative or other ancillary proceedings, particularly where, as was not the case in *Webb* but is true here, the trial court exercised its discretion to award fees in favor of the prevailing party. Subsequent to *Webb*, the high court has held that fees incurred in administrative proceedings are recoverable. (*N.C. Dept. of Transp. v. Crest St. Council* (1986) 479 U.S. 6, 15 [107 S.Ct. 336, 341-342, 93 L.Ed2d 188.]) Later, in *Sullivan v. Hudson* (1989) 490 U.S. 877 [109 S.Ct. 2248, 104 L.Ed.2d 941], the court indicated that fees may be awarded under the Equal Access to Justice Act (28 U.S.C. § 2412) for legal work performed in ancillary administrative proceedings if the administrative proceedings are "so intimately connected with judicial proceedings as to be considered part of the 'civil action' for purposes of a fee award." (490 U.S. at p. 892 [109 S.Ct. at p. 2253], citing *Webb, supra,* 471 U.S. 234; *Pennsylvania v. Del Valley Citizens' Council* (1986) 478 U.S. 546 [106 S.Ct. 3088, 92 L.Ed.2d 439]; and *New York Gaslight Club, Inc. v. Carey* (1980) 447 U.S. 54 [100 S.Ct. 2024, 64 L.Ed.2d 723].)

In any event, California case law clearly provides a trial court discretion to award a fee that compensated work performed in a collateral action that may not have been absolutely necessary to the action in which fees are awarded but was nonetheless closely related to the action in which fees are sought and useful to its resolution. In *Wallace v. Consumers Cooperative of Berkeley, Inc.* (1985) 170 Cal.App.3d 836 [216 Cal.Rptr. 649], the superior court awarded attorney fees under section 1021.5 to consumer groups which successfully challenged the validity of mandatory minimum retail milk prices. The litigation resulted in a settlement agreement providing that if the Director of the Department of Food and Agriculture conducted administrative hearings and suspended

minimum prices by a certain date and dismissed a "companion action" seeking civil penalties against the plaintiff Consumers Cooperative upon the payment of $500, the plaintiffs would drop their judicial challenge as moot. After the administrative hearings were held, the director issued an order suspending minimum retail milk price regulations and also dismissed the companion judicial action for civil penalties of $19,000. The question on appeal was the propriety of the superior court order granting the plaintiffs an attorney fee award which included compensation for services rendered in both the administrative proceedings and the separate judicial action seeking civil penalties. The Court of Appeal affirmed. As to the administrative proceedings, the court noted that under federal law "the hours reasonably expended on an action may include services performed in closely related administrative proceedings." (*Id.* at p. 847, citing *Chrapliwy v. Uniroyal, Inc.* (7th Cir. 1982) 670 F.2d 760.)

The court also discussed the opinion of the United States Supreme Court in *Webb v. Dyer County Bd. of Ed., supra,* 471 U.S. 234, which had just been decided, because that opinion emphasized the highly discretionary nature of the determination whether hours were reasonably expended upon an action. (*Wallace v. Consumers Cooperative of Berkeley, Inc., supra,* 170 Cal.App.3d at p. 848.) The court stated that while the *Webb* court "held that the trial court did not abuse its discretion in denying the fees requested, the clear implication of its decision is that on a proper showing, the time 'reasonably expended' on an action may include time spent on related administrative proceedings." (*Ibid.*) Because the *Consumers Cooperative* court agreed that the related administrative proceedings "were both useful and necessary to the ultimate resolution of the action, and directly contributed to that resolution . . . it was well within the range of the trial court's discretion to determine that the attorney time expended in the administrative hearings was in effect time 'reasonably expended' in the action itself." (*Id.* at pp. 848-849.)

The Court of Appeal also concluded that the fee award properly included time spent by the plaintiffs' counsel on the civil penalty action, which was not only a separate judicial proceeding but one in which the plaintiffs did not prevail. The fact that the civil penalty action was a separate proceeding was no bar, the court stated, because "a trial court may, in its discretion, determine that time reasonably expended on an action includes time spent on other separate but closely related court proceedings." (*Id.* at p. 849, citing *Bartholomew v. Watson* (9th Cir. 1982) 665 F.2d 910, 912-914 and *Brown v. Bathke* (8th Cir. 1978) 588 F.2d 634, 638.) The fact that the plaintiffs did not prevail in the civil penalty action also presented no bar to an attorney fee award compensating them for time spent in defending the action. Although one of the plaintiffs was required to pay a $500 penalty, the plaintiffs did succeed overall on the most significant issue—the validity of mandatory minimum retail milk prices in the state—and a plaintiff who is successful on only some claims may nonetheless be entitled to recover fees for services on the unsuccessful claims. *(Wallace,* citing *Hensley v. Eckerhart, supra,* 461 U.S. 424, 433 [103 S.Ct. 1933, 1939]; cf. *Californians for Responsible Toxics Management v. Kizer* (1989) 211 Cal.App.3d 961, 971 [259 Cal.Rptr. 599] [affirming trial court denial of fees on ground ancillary administrative proceeding " 'was totally unrelated to the direction taken by this lawsuit' "] and *Ciani v. San Diego Trust & Savings Bank* (1994) 25 Cal.App.4th 563, 576 [30 Cal.Rptr.2d 581] [affirming the denial of fees because collateral administrative proceedings "were in no way useful or necessary nor did they directly contribute to the resolution of" the judicial proceeding].)

The principles articulated in the cases just discussed allow a trial court discretion to award fees in circumstances such as those presented in this case. The ancillary judicial proceedings with which we are here concerned related very directly to the issues presented in the action in which fees were awarded, and

respondents prevailed in those proceedings. While the federal proceedings may not have been a necessary precondition of the superior court action, they materially contributed to the resolution of the constitutional issues presented to that court. The federal rulings not only relieved the superior court of burdensome adjudicative responsibilities it would otherwise have had to undertake but diminished the work required of counsel. Furthermore, the trial court exercised its discretion whether to award fees in favor of, not against, the prevailing party. Because a ruling whether fees should be awarded requires, "an intensely factual [and] pragmatic" inquiry *(Crawford v. Board of Education* (1988) 200 Cal.App.3d 1397, 1407 [246 Cal.Rptr. 806]), it is entitled to great respect and may be set aside as an abuse of discretion only if the record provides no basis for the ruling. As the record in this case provides a reasonable basis for including hours spent in the federal proceedings in the fee award, the inclusion of such hours, was within the scope of the trial court's discretion.[18]

2.

(19) DHS claims, finally, that the fee award is excessive because the hourly rate and number of compensable hours allowed by the court were inflated and unjustified. As we earlier pointed out, and DHS acknowledges, an experienced trial judge is in a much better position than an appellate court to assess the value of the legal services rendered in his or her

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18. It is worth noting that DHS has not challenged the inclusion of time spent in the federal proceedings on the ground that the claims in that case were based on federal statutes that do not authorize fees, and there is no other basis upon which they could have been awarded in the federal proceedings. Suffice it for us to note that California courts have awarded fees for all work on a particular issue that is relevant to both claims for which fees are authorized by statute and those to which fees are not statutorily authorized. (See Pearl, Cal. Attorney Fee Awards (Cont.Ed.Bar 2d ed. 2001) § 12.17, p. 291 and cases there cited.)

court, and the amount of a fee awarded by such a judge will therefore not be set aside on appeal absent a showing that it is manifestly excessive in the circumstances. *(PLCM Group v. Drexler, supra,* 22 Cal.4th 1084, 1095.) Such a showing has not been made in this case.

The voluminous materials provided by respondents' counsel in support of the motion for attorney fees provides ample support for the hourly rates they requested and the number of hours for which they sought compensation. The average hourly rate set by the court, $380, reflects a determination that lead counsel, Michael S. Sorgen, was entitled to a rate of $395 per hour and his co-counsel, Dean L. Johnson, was entitled to a rate of $365 per hour. The trail court stated, and the record shows, that respondents' counsel are "highly competent." Attorney Sorgen has been a member of the bar for more than 30 years. During that period he has been lead counsel in numerous class actions and other precedent-setting cases in federal and state courts and has also served as an adjunct or visiting professor of law at Boalt Hall School of Law, Hastings College of the Law and other law schools. Attorney Johnson has held faculty appointments in health care administration at colleges or universities in California and elsewhere, and has practiced law for 10 years. A specialist in health care reimbursement, he has litigated more than 150 cases pertaining to this rather recondite subject. It is obvious from the record that Johnson's expertise materially assisted the court and facilitated adjudication of this complex case.

Respondents submitted the declarations of experts in the areas of court awarded attorney fees and health care reimbursement litigation who attested that the hourly rates requested by respondents' attorneys were in line with market rates charged during the period between 1993 and 2000 by lawyers practicing in the San Francisco Bay Area on a noncontingent basis with varying levels of skills and experience,

and rates allowed by federal and state courts in comparable cases to attorneys with levels of experience comparable to those of respondents' counsel. The declarations included extensive verifiable information regarding rates allowed by courts for counsel to successful plaintiffs in numerous specific complex civil cases litigated in Northern California during 1994 through 1999, including the years of experience of the attorneys, paralegals and law clerks whose hourly rates were judicially set. The foregoing evidence, which DHS has not disputed,[19] demonstrates that the hourly rates allowed by the trial court are within the range of reasonable rates charged by and judicially awarded comparable attorneys for comparable work.

DHS has also failed to show that the number of compensable hours allowed was unreasonably excessive. Respondents produced detailed time records describing, under oath, the number of hours they spent on the case and the nature of the work performed. Attorneys Sorgen and Johnson appear to have efficiently divided the work. Sorgen took the lead in handling the legal and procedural issues and Johnson focused upon the technical health care reimbursement issues. DHS challenges the reasonableness of the time they spent on the case by simply counting up the pages of the numerous pleadings and memoranda respondents submitted over the course of the litigation, many of which are notably short and to the point, and arguing that the length of the submissions does not justify the time taken to prepare them. The example DHS finds most

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19. DHS relies almost entirely on language in *Finkelstein v. Bergna* (N.D.Cal. 1992) 804 F.Supp. 1235, suggesting that a blended rate of $250 per hour was proper because it took into account the fact that work performed by lower level associates should not be compensated at the premium rate a partner could command. We have no quarrel with the reasoning of the court in that case, but note that adjusting $250 for the inflation that has occurred during the decade that has passed since *Finkelstein v. Bergna* was decided would produce a rate not much different from that awarded in this case.

egregious is the complaint, which is only six pages long. Respondents' counsel spent 39 hours preparing this document, which DHS says any competent lawyer could draft in an hour or two. We reject this analysis. The length of a document is no gauge of the time needed to prepare it. The pithy pleadings that are most effective usually require more time to prepare than the endlessly discursive and digressive documents judges often receive. Moreover, given the complexities of this case, the precise language of the concise complaint warranted the exceptional attention counsel devoted to its preparation. Judicial use of the length of a pleading or brief as a measure of the time necessary to prepare it would, reward verbosity and penalize thoughtful and precise draftsmanship. Given the ponderous plethora of prolix pleadings that inundate our courts, no trial judge in his or her right mind would adopt such an approach.

The number of compensable hours allowed by the trial court was reasonable and well within the scope of its discretion.

VI.

Disposition.

For the foregoing reasons, the amount of prejudgment interest awarded by the court is reduced from 10 percent to 7 percent; in all other respects, the judgment is affirmed. Respondents are awarded costs on appeal.

Lambden, J., and Ruvolo, J., concurred.

Supreme Court
FILED
Aug. 14, 2002
Frederick K. Ohlrich, Clerk

Court of Appeal, First Appellate District,
Division Two - No. A094061
S106950

IN THE SUPREME COURT OF CALIFORNIA

En Banc

CHILDREN'S HOSPITAL AND MEDICAL CENTER et al.,
Plaintiffs and Respondents,

v.

S. KIMBERLY BELSHE et al., Defendants and Appellants.

Petition for review DENIED.

GEORGE
Chief Justice

CONSTITUTION

of the

STATE OF CALIFORNIA

As Last Amended November 7, 2000

CALIFORNIA LEGISLATURE
ASSEMBLY
2001-2002

ARTICLE I

Sec. 7. (a) A person may not be deprived of life, liberty, or property without due process of law or denied equal protection of the laws; provided, that nothing contained herein or elsewhere in this Constitution imposes upon the State of California or any public entity, board, or official any obligations or responsibilities which exceed those imposed by the Equal Protection Clause of the 14th Amendment to the United States Constitution with respect to the use of public school assignment or pupil transportation. In enforcing this subdivision or any other provision of this Constitution, no court of this State may impose upon the State of California or any public entity, board, or official any obligation or responsibility with respect to the use of pupil school assignment or pupil transportation, (1) except to remedy a specific violation by such party that would also constitute a violation of the Equal Protection Clause of the 14th Amendment to the United States Constitution, and (2) unless a federal court would be permitted under federal decisional law to impose that obligation or responsibility upon such party to remedy the specific violation of the Equal Protection Clause of the 14th Amendment of the United States Constitution.

Except as may be precluded by the Constitution of the United States, every existing judgment, decree, writ, or other order of a court of this State, whenever rendered, which includes provisions regarding pupil school assignment or pupil transportation, or which requires a plan including any such provisions shall, upon application to a court having jurisdiction by any interested person, be modified to conform to the provisions of this subdivision as amended, as applied to the facts which exist at the time of such modifications.

In all actions or proceedings arising under or seeking application of the amendments to this subdivision proposed by the Legislature at its 1979-80 Regular Session, all courts, wherein such actions or proceedings are or may hereafter be pending, shall give such actions or proceedings first precedence over all other civil actions therein.

Nothing herein shall prohibit the governing board of a school district from voluntarily continuing or commencing a school integration plan after the effective date of this subdivision as amended.

In amending this subdivision, the Legislature and people of the State of California find and declare that this amendment is necessary to serve compelling public interests, including those of making them most effective use of the limited financial resources now and prospectively available to support public education, maximizing the educational opportunities and protecting the health and safety of all public school pupils, enhancing the ability of parents to participate in the educational process, preserving harmony and tranquility in this State and its public schools, preventing the waste of scarce fuel resources, and protecting the environment.

[*Privilege and Immunities*]

(b) A citizen or class of citizens may not be granted privileges or immunities not granted on the same terms to all citizens. Privileges or immunities granted by the Legislature may be altered or revoked. [*As amended November 6, 1979.*]

Supreme Court, U.S.
FILED
DEC 5 2002

No. 02-840

In The Supreme Court of the United States

DIANA BONTA´, DIRECTOR, CALIFORNIA DEPARTMENT OF HEALTH SERVICES,

Petitioner,

v.

CHILDREN'S HOSPITAL AND HEALTH CENTER, et al.,

Respondents.

On Petition For Writ Of Certiorari To The California Supreme Court

OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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INTRODUCTION

The petitioner in this action is the California Department of Health Services ("DHS" or "petitioner"), the entity responsible for administering the Medi-Cal program. The respondents are 11 out-of-state hospitals located in Nevada, Oregon, and Arizona that have provided services in their own states to California residents covered by the Medi-Cal program.

At the trial, the respondents presented detailed evidence supporting the trial court's factual determinations, all of which the California court of appeal affirmed. Based on those facts, the California courts concluded that petitioner's out-of-state reimbursement plan was so grossly inequitable and discriminatory that it violated the Commerce Clause and the Equal Protection provisions of both the California Constitution and the U.S. Constitution.

In its petition, the DHS makes the same arguments that it made in the California courts, all of which have been soundly rejected at every level.

REASONS TO DENY THE PETITION

There are many reasons why DHS' petition should be denied.

I.

THE DECISIONS OF THE CALIFORNIA COURTS DO NOT CONFLICT WITH ANY OTHER COMMERCE CLAUSE DECISION

Some of the crucial factual determinations that the California courts used to support the conclusion that petitioner's reimbursement scheme was irrational, arbitrary and discriminatory are as follows:

- Out-of-state hospitals serve Medi-Cal patients who are much more costly to treat than the Medi-Cal patients treated by in-state hospitals.

- Regardless of the financial disincentives in treating Medi-Cal patients, out-of-state hospitals cannot refuse to treat most Medi-Cal patients or transfer them to a California hospital.

- DHS' payments to out-of-state hospitals have nothing to do with costs, acuity, or any of the other important factors that are considered for in-state hospitals.

- During a five-year time period the costs incurred by the respondent hospitals for treating Medi-Cal patients were $22,660,318, but the compensation the respondents received for those services was only $14,696,955, leaving a net cost shortfall of $7,963,363.

- In-state hospitals are entitled to challenge DHS' cost determinations administratively and judicially, and DHS is obliged to pay interest on the amounts in-state hospitals are ultimately determined to have been under-compensated, but

> out-of-state hospitals cannot similarly challenge the adequacy of the compensation they receive.

Pet. App. at 18a and 19a.

According to the California court of appeal, the "DHS annually distributes over $2 billion in disproportionate share adjustments to state hospitals, but 'has never made a payment of disproportionate share moneys to any out-of-state hospital'" Pet. App. at 18a. The DHS continued to exclude out-of-state hospitals from its disproportionate share program even after the holding in *Children's Hospital and Health Center v. Belshe,* 188 F.3d 1090 (9th Cir. 1999), that such an exclusion violated federal law.

The California courts found not only that petitioner's out-of-state reimbursement scheme was facially unfair, but that the manner in which the petitioner implements it exacerbates that unfairness. The petitioner uses an unweighted average instead of a weighted average as the basis for reimbursing out-of-state hospitals, which results in out-of-state hospital reimbursement rates that are 23.8 percent lower than the rates paid in-state hospitals. Pet. App. at 18a. Also, by using a rate that is set on December 1, and not adjusted until the next year, the petitioner pays out-of-state hospitals even less than the "current" average contract rate mandated by California Welfare & Institutions Code section 14105.15(i). *Id.*

Thus, through an interpretation of California Welfare & Institutions Code section 14105.15(i) that the California courts found to be illegal, DHS augments the already discriminatory burden that its reimbursement scheme

imposes on the respondents, which makes even more compelling the Constitutional violations.[1]

This Court should not grant certiorari to review the foregoing factual determinations.

These factual determinations are particularly significant in the context of the Commerce Clause. In such cases, "where discrimination is patent, . . . neither a widespread advantage to in-state interests nor a widespread disadvantage to out-of-state competitors need be shown" in order to invalidate the law. *New Energy Co. of Indiana v. Limbach*, 486 U.S. 269, 276 (1988). Also, according to well-established precedent "[a]ctual discrimination, wherever it is found, is impermissible, and the magnitude and scope of the discrimination have no bearing on the determinative question whether discrimination has occurred." *Associated Industries of Mo. v. Lohman*, 511 U.S. 641, 650 (1994).

Because there are no facts that support its position, petitioner makes a variety of legal arguments that border on the ridiculous, such as the claim that this case does not involve interstate commerce.

As the court of appeal correctly notes, "the Supreme Court's definition of interstate commerce is notably capacious." Pet. App. at 28a. As used in the U.S. Constitution, the term "commerce" is a "term of largest import."

---

[1] Despite the undisputed findings of the California courts that the petitioner is underpaying out-of-state hospitals by not properly applying Welfare & Institutions Code section 14105.15(i), the petitioner has the effrontery to claim that it is paying out-of-state hospitals the maximum permitted by the statute, and that it could legally pay them much less. Pet. at 3, fn. 2.

Welton v. Missouri, 91 U.S. 275, 279 (1875). It "comprehends traffic, intercourse, trade, navigation, communication, the transit of persons and the transmission of messages by telegraph – indeed, every species of commercial intercourse among the several States . . . " *Adair v. United States*, 208 U.S. 161, 177 (1908). Transactions "may be commerce though illegal and sporadic, and though they do not utilize common carriers or concern the flow of anything more tangible than electrons and information." *United States v. South-Eastern Underwriters Ass'n*, 322 U.S. 533, 549 (1944).

Respondents are clearly engaged in the business of interstate commerce. Over the time period for which they requested damages, the respondent hospitals provided at their facilities in Nevada, Oregon, and Arizona over $22 million of medical goods and services to Medi-Cal beneficiaries from California. Pet. App. at 19a. The treatment of those patients necessarily involved persons crossing state lines, which has long been recognized as a form of commerce. *Camps Newfoundland/Owatonna, Inc. v. Town of Harrison*, 520 U.S. 564 (1997). Also, medical records, insurance information, and patient-related information about those patients moved across State borders. Of course, money from California – meager as it was – flowed from California to hospitals in other states.

Thus, there is interstate commerce.

Despite the overwhelming evidence of petitioner's discrimination against out-of-state hospitals, all of which was unrefuted, the petitioner has the gall to assert that the court of appeal found that California "must *favor* out-of-state hospitals over in-state institutions." Pet. at 9,

original italics. Petitioner's characterization of the court of appeal decision is highly flawed.

To the extent the California courts found that respondent hospitals were entitled to higher reimbursement rates, it was not because they are located out-of-state, as the petitioner contends, but because they treated Medi-Cal patients who were demonstrably sicker (and therefore more expensive to take care of) than the Medi-Cal patients treated at in-state hospitals:

> DHS's reimbursement scheme obviously discriminates against out-of-state hospitals like respondents' that treat significant numbers of Medi-Cal patients. DHS's argument that the scheme is fair, boils down to no more than the false assertion that paying out-of-state hospitals the average of what DHS pays in-state hospitals with which it has contracts simply means that "out-of-state hospitals will receive less than some California contract hospitals receive and more than others do." This superficial argument ignores findings and substantial evidence that the "cost-mix" of Medi-Cal patients cared for by respondent hospitals is considerably higher than that of the in-state hospitals with which DHS contracts, so that the average rate paid such in-state hospitals is an invidious basis upon which to calculate the level of reimbursement that will fairly compensate respondents.

Pet. App. at 23a and 24a.

At the trial, respondents presented substantial evidence of the higher acuity of the Medi-Cal patients they

treat.[2] In the health care field, diagnostic related groups, or "DRGs," measure the acuity of a patient. As the court of appeal notes, "the trial court found that the average DRG weight of Medi-Cal patients treated by respondent hospitals was 'much higher' than that of the Medi-Cal patients treated by in-state hospitals with which DHS has contracts." Pet. App. at 21a, fn. 12.

Thus, this case is not analogous to *Camps Newfoundland/Owatonna, Inc. v. Town of Harrison*, 520 U.S. 564 (1997) or *New Energy Company of Indiana v. Limbach*, 486 U.S. 269 (1988). Pet. at 7 and 8. In those cases, the goods or services being provided were exactly the same. In-state and out-of-state campers received the same services in *Camps*. Ethanol produced in Ohio is identical to ethanol produced out-of-state. Here, however, the Medi-Cal services being rendered at the respondent out-of-state hospitals are much more complicated and costly than the Medi-Cal services being rendered at in-state hospitals.[3]

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[2] It would be a mistake to attach any significance to petitioner's statement that respondents are paid at a rate higher than that received by 58% of in-state contract hospitals because the DRG weight (and hence cost) of the Medi-Cal patients treated by respondent hospitals is much higher, in many cases two to three times higher, than that of the Medi-Cal patients treated by in-state hospitals with which DHS has contracts. Furthermore, out-of-state hospitals are not "in the same position as California hospitals which provide 90% of hospital inpatient services under Medi-Cal," as petitioner contends, because out-of-state hospitals treat much sicker patients than those typically treated at in-state contracting hospitals yet are not permitted to negotiate hospital-specific rates for the services they provide.

[3] Although petitioner claims that the decision in this case will mean that out-of-state entities will be entitled to have their

(Continued on following page)

Petitioner cites *Pike v. Bruce Church*, 397 U.S. 137 (1970) and claims, "the effect [of its rate scheme] is incidental and is far outweighed by the benefits of the payment system." Pet. at 10. However, as the facts set forth above clearly establish, the California courts did not find the petitioner's rate scheme had only "incidental effects," nor did it find any "benefits of the payment system." Furthermore, the *Pike* balancing test does not even apply because petitioner's rate scheme is invalid on its face and thus subject to the strictest judicial scrutiny: " . . . the total indifference of DHS to the true cost of care provided by out-of-state hospitals which serve significant numbers of Medi-Cal patients, and the denial to such hospital of any effective way to seek and obtain the administrative and judicial relief made available to in-state hospitals is facially untenable." Pet. App. at 25a.

II.

DHS IS ACTING AS A MARKET REGULATOR RATHER THAN A MARKET PARTICIPANT

It is clear that in controlling the rates to be paid to out-of-state hospitals for the services they are compelled to provide to Medi-Cal beneficiaries that the DHS is acting as a market regulator rather a market participant.

As the court of appeal correctly notes, "the state is not itself a consumer of the service in question, nor does it pick and choose service providers." Pet. App. at 31a.

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transportation costs taken into account, that is not what the lower court held in this case, nor would such a claim be cognizable under the Medicaid Act or the California Medi-Cal program.

Instead of operating as a market participant, in setting out-of-state rates the DHS is simply "[d]ischarging conventional regulatory responsibilities imposed on it by state and federal law." *Id.* As a result, "[t]he level of reimbursement DHS allows is clearly not responsive to market forces." Pet. App. at 32a. Furthermore, "as DHS itself correctly points out in a different connection, there is no genuine private market regarding the delivery of care to Medi-Cal patients in which the state could participate." *Id.*

Petitioner relies upon *Big County Foods v. Board of Education,* 952 F.2d 1173 (9th Cir. 1992), a case in which a state statute permitted a school district to purchase dairy products if the price of the products were no more than 7% higher than the price of products of like quality produced outside the state. Based on that statute, the school district purchased milk from an Alaskan supplier even though the cost of the milk was higher than the bid submitted by an out-of-state supplier.

Big Country Foods did not involve, as this case does, forced compliance with another state's reimbursement scheme. If the out-of-state supplier in *Big Country Foods* had instead been compelled to provide milk at a substantially lower price than its own cost to produce that milk (in this case, the respondent hospitals are being compelled to provide Medi-Cal services for which they receive only 65% of their costs) then the facts would be similar to the instant case, but no such compulsion existed in *Big Country Foods.*

More instructive are several decisions involving compelled compliance with a governmental scheme. In *SSC Corp. v. Town of Smithtown,* 66 F.3d 502 (2nd Cir. 1995) the court held that a town is engaging in market

regulation, not market participation, when it threatens garbage haulers with criminal fines and jail terms if they fail to do business with it. In *Atlantic Coast Demolition & Recycling, Inc. v. Board of Chosen Freeholders,* 48 F.3d 701 (3d Cir. 1995) the court rejected the argument that a flow control ordinance constituted market participation where the county required garbage haulers to buy landfill services from the county. And, in *Washington State Bldg. & Constr. Trades v. Spellman,* 684 F.2d 627 (9th Cir. 1982) the court rejected the market participation characterization of a program that relied on civil and criminal penalties that only a state could enforce.

III.

PETITIONER'S EQUAL PROTECTION ARGUMENT SHOULD BE REJECTED

Petitioner's equal protection argument should be rejected for two reasons: (1) the Supreme Court does not have jurisdiction to review, in this state appeal, the application of the equal protection clause of the California Constitution and (2) there is no rational basis for petitioner's highly discriminatory out-of-state reimbursement scheme.

The California court of appeal relied upon both the State Constitution and the federal Constitution as the bases for its decision.[4] Pet. App. at 32a-37a. Because the

[4] The California court of appeal also found that petitioner's out-of-state rates violate California Welfare & Institutions Code section 14105.15(i), which is another adequate and independent state ground for its decision.

lower court's decision clearly depends upon both federal and state law, this Court should not upset that judgment. See *Jankovich v. Indiana Toll Road Comm'n*, 379 U.S. 487 (1965); *Minnesota v. National Tea Co.*, 309 U.S. 551 (1940); *Fox Film Corp. v. Muller*, 296 U.S. 207 (1935).

The sound policy behind this rule was well articulated by Mr. Justice Jackson in *Herb v. Pitcairn*, 324 U.S. 117 (1945):

> This Court from the time of its foundation has adhered to the principle that it will not review judgments of state courts that rest on adequate and independent state grounds. The reason is so obvious that it has rarely been thought to warrant statement. It is found in the partitioning of power between the state and federal judicial systems and in the limitations of our own jurisdiction. Our only power over state judgments is to correct them to the extent that they incorrectly adjudge federal rights. And our power is to correct wrong judgments, not to revise opinions. We are not permitted to render an advisory opinion, and if the same judgment would be rendered by the state court after we corrected its views of federal laws, our review could amount to nothing more than an advisory opinion.

Id. at 125-126 (citations omitted).

The cases cited by the petitioner have no relevance to this case. In *New York v. Class*, 475 U.S. 106 (1986), the Supreme Court inferred that the lower court believed the statutory issue insufficient to resolve the case because of its discussion of the constitutional ground. In *Delaware v. Prouse*, 440 U.S. 648 (1979), the state court felt compelled by what it understood to be federal constitutional

considerations to construe its own law in the manner it did. And, in *Zacchini v. Scripps-Howard Broadcasting Co.*, 433 U.S. 562 (1977), the lower court did not mention the State Constitution, but instead relied upon the Supreme Court's First Amendment cases as controlling. None of the above-described facts apply to this situation.

Of course, if the Supreme Court believes it is unclear whether the California court of appeal relied on the State equal protection provision in reaching its decision, then it should be asked, rather than told, what it has intended:

> it seems consistent with the respect due the highest courts of states of the Union that they be asked, rather than told, what they have intended. If this imposes an unwelcome burden, it should be mitigated by the knowledge that it is to protect their jurisdiction from unwitting interference as well as to protect our own from unwitting renunciation.

Herb v. Pitcairn, 324 U.S. at 128 (1945); see also *California v. Krivda*, 409 U.S. 33 (1972); *Mental Hygiene Dept. v. Kirchner*, 380 U.S. 194 (1965).

At the trial, the DHS did not produce any evidence of a legitimate government purpose for distinguishing between hospitals based on location. Despite no support in the record for its discriminatory reimbursement scheme, DHS argues in its petition to this Court that there would be administrative problems created by attempting to apply to out-of-state hospitals the methods used to pay in-state hospital. Pet. at 19-22. However, as the court of appeal correctly notes, that argument is a red herring because the respondents never proposed that they be treated in exactly the same manner as in-state hospitals:

> DHS's argument that there is no workable alternative to the reimbursement scheme it began using in 1992 consists of little more than an explanation of the practical impossibility of treating out-of-state hospitals in exactly the same manner as in-state hospitals. The argument posits a straw man. Respondents have never proposed that they be treated in exactly the same manner as in-state hospitals. All they sought, and all the trial court ordered, was that DHS revert to the reimbursement scheme prescribed by DHS regulations in effect prior to the enactment of subdivision (i) in 1992 (tit. 22, former § 51543 (1992)), which had been approved by the HCFA and which DHS employed for many years without complaint.

Pet. App. at 35a and 36a. Petitioner did not show, and cannot show, that the reimbursement scheme it applied to out-of-state hospitals for many years prior to the enactment of Welfare & Institutions Code section 14105.15(i) lacks a rational basis.

IV.

THE DECISION IN THIS CASE IS NOT OF NATIONAL IMPORTANCE

This case is not of national importance.

The California court of appeal decision that petitioner seeks review of is binding precedent only in the First District of the court of appeal of the State of California.

Also, many states already successfully apply in-state procedures to high volume out-of-state hospitals like respondents, thereby avoiding the type of disparate treatment that the California courts found to be facially discriminatory.[5]

CONCLUSION

For the foregoing reasons, respondents respectfully request that the petition for a writ of certiorari be denied.

Respectfully submitted,

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[5] For example, in Georgia high volume out-of-state providers are actually enrolled into Georgia's Medicaid program and are subject to the same administrative requirements imposed on in-state hospitals. Commerce Clearinghouse (CCH) Medicare and Medicaid Guide, 2000, ¶15,574. Illinois applies its in-state procedures to out-of-state hospitals that provide 100 days or more of service to persons covered by the Illinois Medical Assistance Program. Ill. Adm. Code 148.310 (2001). Montana applies its in-state procedures to out-of-state facilities located no more than 100 miles outside of Montana. CCH Medicare and Medicaid Guide, 2000, ¶15,608. And, Idaho applies its in-state procedures to out-of-state hospitals with $50,000 or more of Idaho charges. IDAPA 16.03.10.456 (2000).